FOREIGN OPERATIONS, EXPORT FINANCING, AND RELATED PROGRAMS APPROPRIATIONS FOR 1991

HEARINGS

BEFORE A

SUBCOMMITTEE OF THE

COMMITTEE ON APPROPRIATIONS
HOUSE OF REPRESENTATIVES

ONE HUNDRED FIRST CONGRESS

SECOND SESSION

SUBCOMMITTEE ON FOREIGN OPERATIONS, EXPORT FINANCING, AND RELATED PROGRAMS

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[1] Resigned Committee, May 16, 1990.

[2] Elected to Committee, May 24, 1990.

FOREIGN OPERATIONS, EXPORT FINANCING, AND RELATED PROGRAMS APPROPRIATIONS FOR 1991

WEDNESDAY, MARCH 21, 1990.

STRENGTHENING U.S. ECONOMIC OPPORTUNITIES

WITNESSES

EUGENE K. LAWSON, FIRST VICE PRESIDENT AND VICE CHAIRMAN, EXPORT-IMPORT BANK

PRISCILLA ROBB-AYERS, DIRECTOR, TRADE AND DEVELOPMENT PROGRAM

JAMES D. BERG, EXECUTIVE VICE PRESIDENT, OVERSEAS PRIVATE INVESTMENT CORPORATION

REGINALD J. BROWN, ASSISTANT ADMINISTRATOR FOR PROGRAM AND POLICY COORDINATION, AGENCY FOR INTERNATIONAL DEVELOPMENT

CHAIRMAN'S OPENING STATEMENT

Mr. OBEY. Good afternoon. Today we are going to be dealing with various programs in the foreign assistance bill which relate to strengthening America's trading and export opportunities.

EXPORT-IMPORT BANK FUNDING

Before we begin, I would like to provide some context for our discussion. In 1981, the United States ran a very small trade surplus. Our economy was shifting more and more into the service sector; a surplus in service exports offset the small deficit in the merchandise trade sector. In the same year, Congress provided about $5.5 billion in direct credits for the Export-Import Bank.

Since 1981, funding for the Bank has, to be polite, taken a nosedive. The Reagan Administration repeatedly tried to eliminate funding. The State Department since '85, when Gramm-Rudman was passed, has apparently found it convenient to cut funding for the Bank in order to provide room in the foreign assistance budget for other programs.

Total foreign aid in 1981 was about $15.5 billion, but in non-Exim accounts it totaled about $8.9 billion. Now for fiscal year 1990 funding totals $14.6 billion for all accounts, but in non-Exim accounts it totals $14 billion, an increase of about 57 percent.

During the same period from 1981 to 1990, Exim funding has dropped from $5.5 billion to $612 million, a cut of about 89 percent—not exactly small potatoes.

The Administration request for fiscal year 1991 further continues that squeeze. The Exim account comes in under the Administration request for a direct credit level of only $500 million, a cut of eighteen percent in one year, while the rest of foreign aid increases about nine percent.

In addition, the Congress provided for a $20 million interest match program which could have financed between $200 million and $250 million in exports in 1990 in addition to the direct credit program of $612 million. But the Administration has decided not to start an I-match program in 1990. It has not requested any authority for it in 1991, despite the fact that the Banking Committee passed legislation last year authorizing a $35 million I-match program for 1991 which could potentially finance an additional $350 million in U.S. exports.

So in summary, the Administration's Exim request for 1991 presents about a 40 percent cut in direct export finance when one considers the refusal to initiate the I-match approach. Additionally, the Administration has requested a cut of about six percent in the Trade and Development Program.

Then, in a request which effectively masks those significant cuts, the Administration, as they did last year, increases its request for Exim guaranteed loans. This has the effect of making the Administration look as if they have increased its total requests for all export-related programs. I do not want to say that is their motive, but that is certainly the effect.

The 1991 guaranteed loan request is for $10.599 billion, an increase of $250 million above the $10.384 billion for the 1990 loan level. But anyone who tracks the situation closely understands that probably less than $6.5 billion of the loan guarantees will actually be used this year. Demand projections will show that no one expects to use this year's request level in 1991.

So the effect of what the Administration has proposed in my judgment is to make it appear as though this budget is in fact, a stimulus to our export capabilities. The fact is it represents in real terms a reduction in our export capabilities, at least those financed through this bill.

In the meantime, we have new export opportunities because of political developments in Eastern Europe and in Panama and Nicaragua. The new Eastern European market may well turn out to be the largest potential new export market since the end of World War II. However, the Administration's budget submission does not demonstrate the fact that we recognize that opportunity. After having said that, I recognize that some people might think it is a biased summary of the situation. I do not think so.

Why do we not now move on to let the Administration witnesses defend the Administration's budget. First we will hear from Mr. Eugene Lawson, First Vice President and Vice Chairman of the Export-Import Bank; then Mrs. Priscilla Rabb-Ayres, Director of the Trade and Development Program; followed by Mr. James D. Berg, Executive Vice President of the Overseas Private Investment Corporation; and then by Mr. Reginald Brown, Assistant Administrator of AID for Program and Policy Coordination.

Mr. Lawson, why do you not start. We will put all of your statements in the record. If you could, summarize your statement in a reasonable amount of time, but leave enough time for us to learn something by your statements.

Please proceed.

MR. LAWSON'S OPENING STATEMENT

Mr. LAWSON. Thank you, Mr. Chairman.

I do have two statements, one long and one short, and as you suggested I will go to the short statement first. Mr. Chairman, members of the subcommittee: I welcome the opportunity to speak to the subcommittee on behalf of the Bush Administration's fiscal year 1991 budget request for Export-Import Bank.

This is a difficult period, in which most domestic and international programs of the Federal government are being required to make budget cut backs. We at Eximbank have tailored our budget request to overall spending limitations and to the need to comply with the provisions of the Gramm-Rudman-Hollings legislation.

Eximbank looks forward to the challenge of operating successfully in an extraordinary and expanded international environment. To achieve our objectives of financing and promoting U.S. exports by operating all our programs, that is loans, guarantees, and insurance, we must have sufficient funding levels and sufficient administrative resources.

The Bush Administration's budget request for fiscal year 1991 includes $500 million for direct loans of the Eximbank. This request is made in recognition of the very limited resources in the international affairs account, the 150 account.

Through the direct credit program, Eximbank addresses gaps in the availability of competitive financing from the private sector for U.S. capital goods exports. We want to ensure that U.S. exporters do not suffer widespread losses of export sales as a result of subsidized financing offered by other foreign governments to their exporters.

We request that up to $114 million of the amount requested for direct loans be made available for the tied aid credit War Chest to counter foreign tied aid mixed credits. This is an increase of $4 million over the $110 million that the Congress appropriated in fiscal year 1990 for this activity.

The issue of tied aid credits will be pursued within the framework of the OECD, but the talks are going to be very long and difficult. There is no question about that, and the U.S. is going to need the leverage of the Bank's War Chest in fiscal year 1991 to achieve progress in these talks.

From fiscal year 1987 to fiscal year 1989, the Bank has used all of its direct loan authority. We expect that the loan authority for fiscal year 1990 of $612.4 million and the requested fiscal year 1991 amount of $500 million will also be entirely used.

The Bush Administration's budget for fiscal year 1991 for the Bank's guarantee and insurance commitments is $10.599 billion. Under our guarantee and insurance programs, the Bank increases commercial financing for U.S. export sales by assuming certain commercial and political risks of non-repayment.

The Bank has also requested $23 million in fiscal year 1991 for administrative expenses. Our request will support a full-time equivalent personnel level of about 336 individuals. Of the amount requested, 75 percent is for personnel compensation and benefits, 10 percent for rent of office space, and about 2 percent for travel. The remaining balance of about 13 percent covers phones, purchases of supplies, et cetera.

I would like to conclude, Mr. Chairman, by bringing the subcommittee up to date on the activities and results of our efforts to reach out to smaller and medium-sized companies through the state and local export finance and development agencies. That is, I want to describe very quickly the Eximbank City/State Program.

In February of 1989, the Bank's Board of Directors approved the City/State Program as a national outreach program. The board's action was based on the significant success achieved with a pilot program of cooperation with the States of California, Maryland and Massachusetts and four other cities.

I am pleased to report, Mr. Chairman, that the City/State Program has expanded to include the States of Washington, Nevada, Texas, Utah, Michigan, and the Port Authority of New York and New Jersey. There has also been interest expressed by six other states.

I am convinced that this is the best way to leverage our very scarce resources, since we have no field offices, so that we can reach out across this huge country and tap into the small and medium-sized businessman.

Thank you for giving me the opportunity to outline our budget, and we look forward to working with the subcommittee and I will be glad to answer any questions you and the subcommittee may have.

[The prepared statement of Mr. Lawson follows:]

STATEMENT OF
EUGENE LAWSON
FIRST VICE PRESIDENT AND VICE CHAIRMAN
EXPORT-IMPORT BANK OF THE UNITED STATES
BEFORE THE
SUBCOMMITTEE ON FOREIGN OPERATIONS
OF THE
COMMITTEE ON APPROPRIATIONS
U.S. HOUSE OF REPRESENTATIVES
MARCH 21, 1990

Mr. Chairman, Members of the Subcommittee:

I welcome the opportunity to speak to the Subcommittee on behalf of the Bush Administration's Fiscal Year '91 budget request for the Export-Import Bank.

This is a difficult period in which most domestic and international programs of the Federal Government are being required to make budget cut backs. Eximbank has tailored our budget request to overall spending limitations and to the need to comply with the provisions of the Gramm-Rudman-Hollings legislation.

As the new decade unfolds, our country is confronted as never before by international economic challenges which will shape the future of America and the rest of the world far into the twenty first century. Our response to change -- in Japan and the Asian NICs, the indebted developing countries, the increasingly integrated European Community, or newly emerging democracies --

can create tremendous opportunities for the American business and banking communities.

The Export-Import Bank is already responding to the needs of newly emerging democracies as diverse as Poland, Czechoslovakia and Panama. In these nations, trade and investment opportunities are essential if a market economy is to take hold. Eximbank's assumption of commercial and political risks enables American banks and exporters to participate in this transformation.

On March 1, 1990, the Bank extended short term export credit insurance to cover U.S. exports to Poland. The insurance is offered through Eximbank's agent, the Foreign Credit Insurance Association (FCIA). Coverage is available for sales to either private or public sector Polish buyers. This Eximbank program complements the proposed $200 million Trade Credit Insurance Program (TCIP) guaranteed by AID. TCIP will be limited by law to supporting sales to private sector buyers. The Bank's new country policy for Poland was adopted in response to the Polish Government's implementation of its historic economic reforms, and the support Poland is receiving from multilateral and bilateral sources.

On March 6, the Bank opened all of its programs to support U.S. exports to Czechoslovakia. We acted just two weeks after President Bush lifted the prohibitions on Eximbank financing by signing a waiver of the Jackson-Vanik amendment, and by issuing a determination that Eximbank support for exports to Czechoslovakia is in the U.S. national interest.

We are particularly pleased to be open in Czechoslovakia as the Czechs have been outspoken in their preference for trade and investment opportunities rather than more traditional forms of foreign assistance. For Eastern Europe as a whole, we estimate that demand for all of our programs will be in the range of $300 to $500 million per year.

Turning for a moment to another region of the world, Eximbank resumed short and medium-term cover for U.S. exports to Panama in mid-February. We believe that in this one country alone, pent up demand for our financing could reach the $400 million level.

Eximbank looks forward to the challenge of operating successfully in an expanded international environment. To achieve our objectives of financing and promoting U.S. exports by operating all our programs -- export loans, guarantees and insurance -- we must have sufficient funding levels and sufficient administrative resources.

DIRECT CREDIT PROGRAM

The Bush Administration's budget request for FY'91 includes $500 million for direct loans of the Export-Import Bank. This request is made in recognition of the very limited resources in the international affairs account.

Through the Direct Credit Program, Eximbank addresses gaps in the availability of competitive financing from the private sector for U.S. capital goods exports. We want to ensure that U.S. exporters do not suffer widespread losses of export sales as a result of subsidized financing offered by other governments to their exporters. Eximbank's Direct Credits are competitive with the financing offered by foreign export credit agencies.

Thus, the Bank permits a foreign buyer's purchasing decisions to be based on market factors -- such as price, technology and service -- rather than the availability of subsidized credit from a foreign government.

We believe that the long-term benefits to the U.S. economy generated by government supported competitive export financing of U.S. capital goods outweigh the subsidy costs of such credits.

The Bank helps to maintain U.S. productivity by allowing free market forces to operate. We ensure that U.S. capital goods industries operate at market-determined -- and **not foreign government determined** -- production levels.

The interest rates charged by Eximbank are the minimum rates allowed under agreement with other member nations of the Organization of Economic Cooperation and Development(OECD). The rates are revised semiannually to reflect changes in the weighted average interest rates on government bond issues in the five major international currencies. The rates for loans of over five years are currently 9.65% for intermediate countries and 8.30% for relatively poor countries. Export Credit Agencies do not offer subsidized lending to rich countries.

Exceptions to the OECD minimum rate structure are allowed for mixed credits, where official aid and an export credit are blended into one financing package.

The Eximbank direct loan program is vitally important to financing exports to countries like India, Indonesia, Algeria and, increasingly, to Central and South America. Official export credit in these developing country markets is vigorously competitive. In fact, in some of these countries, suppliers are often required to bring heavily subsidized or mixed credit financing to the table.

Tied Aid "War Chest"

We request that up to $114 million of the amount requested for direct loans be made available for the tied-aid credit "War Chest" to counter foreign tied aid credits. This is an increase of $4 million over the $110 million Congress appropriated in FY'90.

The issue of tied aid credits will be pursued within the framework of the OECD, but the negotiations will be long and arduous. The U.S. will need the leverage of the Bank's War Chest in FY'91 to achieve progress in the negotiations.

From FY'87 to FY'89, the Bank has used all of its direct loan authority. We expect that the loan authority for FY'90 of $612.4 million and the requested FY'91 amount of $500 million will also be entirely used.

Intermediary Loan Program

Eximbank's Intermediary Loan Program enables responsible parties to extend O.E.C.D. minimum fixed-rate, medium-term or long-term export loans to buyers of U.S. exports that face officially subsidized competition.

Fixed-rate financing is often necessary for a U.S. exporter to obtain a foreign order, yet commercial banks and others are often reluctant to provide fixed interest rates due to fluctuations in their cost of funds over the term of the loan.

Eximbank's medium term Intermediary Loans are structured as "stand-by" loan commitments. The intermediary lender may request disbursement from the Bank at any time during the life of the loan to the foreign buyer.

In FY'89 the Bank authorized $201.7 million of intermediary loans.

GUARANTEE AND INSURANCE PROGRAMS

The Bush Administration's budget request for FY'91 for the Bank's guarantee and insurance commitments is $10.599 billion.

Under our guarantee and insurance programs, the Bank increases commercial financing for U.S. export sales by assuming certain commercial and political risks of non-payment. Since financing is a critical element in many export sales, these programs help U.S. exporters increase their export sales by increasing the availability of financing in private capital markets.

The export credit insurance program encourages additional exports by providing risk protection for those exports requiring short-term (up to 180 days) and medium-term (up to five years) credit terms and for which private sector credit insurance is not available. The capacity of the private sector to offer export credit insurance currently is extremely limited. Thus, the role of the public sector is critically important, especially to small and medium-sized businesses.

Administrative Expenses

The Bank has requested $23,171,000 for FY'91 for administrative expenses.

The administrative expense budget of the Bank provides for personnel, support services, and operating expenses. Our request will support a full-time equivalent personnel level of 336. Of the amount requested, $17,428,000 (75%) is for personnel compensation and benefits, $2,321,000 (10%) is for rent of office space, and $481,000 (2%) is for travel. The remaining balance of $2,941,000 covers such necessary operating expenses as telecommunications, purchases of supplies, support services, equipment leasing and maintenance, printing, postage, and other service contracts.

Loan and Guarantee Loss Reserves

I would like to comment here on the $4.8 billion loan loss reserve which the Bank established for its loan and guarantee portfolio. The establishment of the reserve would not have been possible without your efforts, Mr. Chairman, and those of other members of the authorizing committees. The reserve puts us fully in compliance with the accounting requirements of the G.A.O.

Our action simply revalued some of the loans in the Bank's portfolio and, in no way implies debt forgiveness. We still expect our loans to be repaid in full.

The existence of a reserve will strengthen the Bank and will enhance the Bank's ability to carry forward its export support mission. The focus of debate over the Bank's activities has already shifted away from the question of accounting for the value of old loans to a more productive debate over the many pressing issues currently facing us.

The loan loss reserve is, of course, an accounting change and not a cash transaction. It will not affect the U.S. Government's budget or the FY '91 budget request for Eximbank.

CITY/STATE PROGRAM

I would like to bring the Subcommittee up to date on the activities and results of our effort to reach smaller and medium-sized companies through state and local export finance and development agencies -- the Eximbank City/State Program.

In February of 1989, the Bank's Board of Directors approved the City/State Program as a national outreach program. The Board's action was based in the significant success achieved with a pilot program of cooperation with the states of California, Maryland and

Massachusetts, and with the cities of Los Angeles, CA; Tucson, AZ; Louisville, KY; and Columbus, OH.

The City/State Program offers export counseling and financial assistance to small and medium-sized businesses through nearby state and local agencies. The program also vastly expands our access to small and mid-sized business communities in the participating regions.

I am pleased to report that to date, the City/State Program has generated exports of more than $20 million. We have expanded participation in the Program to include the states of Washington, Nevada, Texas and Michigan. Utah and the Port Authority of New York/New Jersey have recently completed our training. Interest has also been expressed by Louisiana, Pennsylvania, North Carolina, New Mexico and Bridgeport, Connecticut.

The City/State Program has substantially contributed to Eximbank's ability to meet the Congressional Mandate to assist small and medium-sized businesses.

Mr. Chairman, we would like to thank you and the other Members of the Subcommittee for your efforts last year to increase our medium-term sublimit to $215 million. These smaller transactions continue to be a very important part of our overall business and now account for approximately 30% of Eximbank transactions. We estimate that even with the higher sublimit we will reach the ceiling sometime in the fourth quarter of this year.

Thank you for giving me an opportunity to outline our budget request for the coming fiscal year. We look forward to working with the Subcommittee members and staff to meet the challenge facing our exporters in the traditional markets of South America, Asia, and Africa as well as the emerging markets of Eastern Europe and Central America. I will be glad to answer any questions you or members of the Subcommittee may have.

Mr. OBEY. All right.

OPENING STATEMENT OF MS. RABB-AYRES

Mrs. RABB-AYRES. Thank you, Mr. Chairman. Mr. Chairman and members of the subcommittee:

I am pleased to testify today on the Trade and Development Program's efforts to strengthen U.S. economic opportunities. The historic events of the last several months in Eastern Europe and Central America have required swift and constructive action on the part of the U.S. government to encourage and sustain the infant democracies.

Economic development, especially the nurturing of market-based economies, is clearly the essential underpinning of the breathtaking political change. In this context, TDP has been an extremely effective instrument of U.S. foreign policy.

TDP IN POLAND, HUNGARY, AND PANAMA

We have emphasized time and time again that TDP is uniquely suited to respond quickly to Congressional and Administration assistance initiatives, and I believe that we have proven this in an unprecedented fashion in Eastern Europe and Panama. For example, one year ago we were approached by the U.S. embassy in Hungary with a proposal for a project to down-size an inefficient metallurgical complex at Miskolc, in Borsod County. The project also includes a plan to revitalize that depressed industrial region to encourage foreign investment.

TDP was able to respond immediately, and within two months was the first U.S. agency to provide concrete assistance through a feasibility study grant of $500,000 for the Borsod project. This grant was signed during the President's visit to Hungary in July.

The importance of this project to the government of Hungary is apparent in the fact that Hungary contributed $250,000 of its scarce foreign exchange to this project. Ambassador Zeder and other OPIC officials have already pursued TDP's initiative by visiting Miskolc to make a preliminary assessment of the potential investment opportunities there.

With 1990 SEED funds, TDP plans to provide a grant of $525,000 to the Hungarian Ministry of Transport, Communications and Construction for a master plan for a telecommunications digital overlay network and for a technical orientation visit of Hungarian telecommunications officials to the United States.

TDP is also reviewing a request for a national electrical network control and distribution study. Other requests are anticipated from Hungary in the environmental, transportation, and industrial sectors.

TDP was introduced to Poland in September 1989, when Secretary Mosbacher invited me to join his Department of Commerce mission to Warsaw. TDP returned in November at the invitation of the Polish Ministry of Foreign Economic Relations to explore specific project opportunities with the various ministries.

At the same time, TDP also had the opportunity to participate in OPIC's first Poland investment mission. As a result, TDP has plans to fund a $750,000 planning study for telecommunications modernization. TDP is also currently assessing requests for planning assistance in air traffic control modernization and for solid and hazardous waste projects. TDP expects to provide additional assistance in power sector modernization, transportation, and industrial reorganization.

Just three weeks ago, the regional director of TDP and I accompanied an OPIC investment mission to Panama and conducted several independent TDP working sessions with Panamanian ministries. This gave TDP the opportunity to introduce our program to the new Panamanian government at a critical time in their development planning and to meet with select U.S. business people who, by dint of their participation in the OPIC mission, have demonstrated a strong desire to operate in Panama.

During that trip I had the honor of meeting with President Endara, who expressed great enthusiasm for the TDP program.

Upon my return from Panama, a fax from the Vice Minister of Commerce and Industry was waiting for me with a list of nine priority projects which could involve a TDP commitment in Panama of $2 million to $2.5 million. TDP already has approved definitional missions to examine in more detail four of these potential projects.

TDP was greeted with great enthusiasm and optimism by all three new governments. One observation that is frequently made in these countries is that TDP assistance is welcome and particularly attractive as it is offered on a collegial basis, that is in the spirit of cooperation rather than coopting. National pride is respected and nurtured, while highly desired U.S. technical assistance is made available on urgent priority projects.

TDP ACTIVITIES

While other U.S. government assistance efforts are being developed, TDP definitional missions and grants serve to demonstrate the U.S. government's commitment. At the same time, TDP provides the basis upon which programs of other agencies can be effectively launched.

We have often testified as to our role as a catalyst for U.S. business opportunities, and I would like to point out here that we also operate effectively as a catalyst for activities of other U.S. government agencies.

While TDP will expend a great deal of effort this year in Eastern Europe and Central America, I do want to assure you that we will not neglect our responsibilities in other parts of the world.

In addition to TDP's traditional role of funding feasibility studies and other project planning services, we are also emphasizing other activities that will maximize the benefits of TDP funding and directly stimulate U.S. procurement. In some cases, it is appropriate and extremely effective to fund the visit of host government officials to the United States to acquaint them with U.S. technology and equipment and give them an opportunity to meet with U.S. firms.

In fact, we have one such reverse trade mission in Washington this week. We have a delegation of senior level Venezuelan telecommunications officials, and just last night I was at a reception with these officials and I was told that several new opportunities, both for the U.S. and for Venezuela, have been uncovered just in the last couple of days, that were totally unknown prior to the mission.

I have also been assured that the benefits that will be derived from this mission will be multiples of the cost of TDP as far as bringing the mission over.

In other instances, TDP has found that carefully planned and organized conferences and technology seminars can open up valuable business opportunities and can be an extremely efficient means of achieving TDP's mission. TDP has encouraged the States to participate in conferences and technology seminars where such involvement can enhance TDP's efforts to benefit State exports.

For example, in November of '89 TDP funded the Conference on Asia-Pacific Petrochemical and Refinery Integration, otherwise called "CAPRI," which is much easier to say. This was in Houston. CAPRI was organized by the State of Texas, the East-West Center in Hawaii, and the University of Houston's Small Business Development Center.

The purpose of CAPRI was to bring together senior industry and government decisionmakers from the U.S. and Asia to discuss regional petrochemical markets and development prospects for the 1990s. The potential investment opportunities identified during this conference have been estimated at $20 to $22 billion overall.

TDP also works closely with State development agencies as a prime mechanism to disseminate information on export opportunities to U.S. firms. This year, TDP made a grant of $100,000 to the State of Illinois Export Council to perform several buyers missions to assist Illinois manufacturers, suppliers, and service companies to export to Poland. The State Legislature contributed $124,000 to this effort.

Also this year, TDP provided a grant for $302,000 to the Wisconsin Department of Development to co-fund the promotion of U.S. exports by establishing a state-wide trade lead program and by building a network of trained trade development personnel to provide assistance in export and trade development for the business community.

TDP's activities may also complement U.S. government initiatives not directly or primarily associated with trade. We in fact funded a $2 million study in Bolivia. This was a minerals and mining study. Development of the mining sector in Bolivia offers tremendous opportunities for U.S. business and at the same time offers alternative employment opportunities to Bolivian people that are now working in the cocoa fields. We are trying to get them back into the mines. This fits very well into the anti-drug initiative in the Andean region.

Through fiscal year 1988, TDP has obligated a total of $113 million for planning major projects. Although TDP grants are untied to follow-on procurement, nearly $3 billion of exports have been associated with projects supported by TDP-funded studies to date.

Moreover, these figures are only the tip of the iceberg. It can take many years to reap the benefits from a feasibility study. The lead time necessary to move large-scale development projects to implementation can run as long as ten to 20 years before final contract negotiations and final backing are concluded.

The bulk of equipment sales will usually come toward the end of a project's implementation.

An independent analysis of exports associated with TDP-funded projects estimates direct follow-on exports of approximately $7 to $8 billion in the next ten years, and this figure does not include exports indirectly attributable to TDP and spin-off projects, which are difficult to document.

U.S. companies who work with TDP gain recognition and an opportunity to introduce U.S. equipment and technologies into new markets. In the international marketplace, companies repeatedly receive offers and contracts for spin-off projects related to their participation on a TDP-funded project. To date, over 400 companies in 40 States and the District of Columbia have benefited from TDP activities.

In closing, I would like to thank Mr. Obey and the members of the subcommittee for their continued interest and enthusiastic support of TDP. On a personal note, I would like to say that I am extremely proud of what TDP is able to accomplish and what we have accomplished so far, and I am also very excited about the challenges ahead of us.

Thank you very much.

[The prepared statement of Ms. Rabb-Ayres follows:]

TESTIMONY OF
PRISCILLA RABB-AYRES, DIRECTOR
U.S. TRADE AND DEVELOPMENT PROGRAM
BEFORE THE
SUBCOMMITTEE ON FOREIGN OPERATIONS
HOUSE COMMITTEE ON APPROPRIATIONS

Mr. Chairman and members of the Subcommittee, I am pleased to testify today on the Trade and Development Program's efforts to strengthen U.S. economic opportunities. My testimony will focus on TDP's FY 1990 program in Eastern Europe, Latin America and worldwide, plans for FY 1991, and the indicators of the program's success.

The Trade and Development Program (TDP), established in 1980, is an independent federal agency under the aegis of the International Development Cooperation Agency (IDCA). TDP has an exclusive mandate to promote U.S. exports for major development projects in middle-income and developing countries. The 1990s promise to be a decade of significant economic and political change, and TDP will respond quickly and effectively to U.S. Government initiatives and priorities in emerging democracies and developing economies.

TDP is successful as a result of its unique characteristics and strengths. TDP projects encourage U.S. firms to participate in sectors and markets that are new to them or otherwise difficult to penetrate without U.S. Government support. TDP's project selection criteria help ensure that projects are of sufficient priority to be implemented. The relationships established by TDP with foreign governments and multilateral development banks enable the U.S. private sector to become involved in the early stages of key development projects that promise substantial short- and long-term market opportunities for U.S. goods and services. Moreover, TDP is able to put into practice the importance placed by the U.S. Government on free market, private sector involvement in the implementation of development projects.

The process of democratization and the development of market-based economies in Eastern Europe presents a vast range of opportunities for U.S. business. TDP will work to facilitate U.S. commercial access to these markets and will assist in the development of private enterprise in this region. TDP is currently active in Poland, Hungary and Yugoslavia, and will initiate programs in other Eastern European countries as U.S. policy allows.

TDP-funded studies and related activities provide a generous return to the U.S. economy. Although TDP grants are untied to follow-on procurement for project execution, over $2.8 billion of U.S. exports have been associated with projects supported by TDP-funded studies. The full measure of exports generated is not yet clear because, typically, project implementation takes many years. It is estimated that over the next decade, projects related to TDP activities financed to date are likely to generate an additional $20 billion in U.S. exports. To date, over 400 companies in 40 states and the District of Columbia have benefited from TDP activities. U.S. business representatives who have participated in TDP-funded activities regard them as important and practical ways to improve their marketing, exposure, and networking for future business activities.

In addition to direct exports, there are significant indirect benefits that are not as easily quantifiable. U.S. companies that participate in TDP-funded feasibility studies are given the opportunity to demonstrate their skills and abilities to foreign officials in-country, and as a result often win additional business without U.S. Government assistance. The business community has supplied TDP with numerous letters documenting such spin-off benefits. For example, as a direct result of a major U.S. engineering firm's work on a TDP-sponsored activity in Africa, a subsidiary of the firm won a $10 million management contract at a power plant not associated with the TDP study.

In FY 1990 and 1991, TDP will continue to promote the participation of U.S. businesses in the development process. In addition to funding feasibility studies and other project planning activities, TDP will fund a variety of complementary activities such as trade-related education and training programs, reverse trade missions, and conferences designed to stimulate the export of U.S. technology, goods, and services. TDP will also pursue effective use of its tied aid authority.

TDP will consider proposals in all industry sectors where U.S. companies are competitive in world markets, but intends to focus on those sectors in which the United States has a particular strategic interest and/or technical competitive edge. Such sectors include telecommunications, energy, transportation, waste management, trade-related training, water and air pollution, and other environmental concerns.

TDP funds feasibility studies, reverse trade missions, training programs, conferences, and other project planning services related to major projects in middle-income and developing countries where there is a potential for exporting U.S. technology, goods, and services. Contracts funded by TDP grants must be awarded to U.S. companies. In addition, TDP is authorized to administer a program of tied aid credits for U.S. exports in cooperation with the Export-Import Bank of the United States.

TDP's involvement in project planning emphasizes the responsiveness of the United States to host country development needs; enhances the position of U.S. suppliers in international competition for follow-on procurement; encourages untied procurement policies in developing countries; and demonstrates U.S. Government support for U.S. private sector participation in development projects around the world.

TDP supports priority projects in host country development plans. The host governments play an active role in developing the scope of work, selecting the U.S. company to carry out the study, and monitoring the progress of the endeavor. TDP's emphasis on host government participation combined with the high degree of professionalism, skill, and objectivity of U.S. companies ensures a satisfactory and useful product. This cooperation also engenders trust between the host country, TDP, and the U.S. business community that often encourages collaboration on future projects.

Factors ranging from U.S. foreign policy objectives to overall budget limitations are considered in project selection. All TDP projects, however, must meet the following specific criteria:

Development Priority: TDP projects must be development priorities of the host country and likely to be implemented. TDP must receive a formal request from the host government, and the U.S. Embassy must endorse TDP's involvement in the proposed project.

U.S. Export Potential: Projects must present an opportunity for substantial sales of U.S. goods or services.

Untied Funding Availability: There must be assurance that untied funding for project implementation will be available and procurement will be open to U.S. firms.

In addition to TDP's traditional role of funding studies and other project planning services, TDP is also emphasizing new activities that will maximize the benefits of TDP funding and directly stimulate U.S. procurement. For example, in some cases, it may be appropriate to fund the visit of host government officials to the United States to acquaint them with U.S. technology and equipment and give them an opportunity to meet with U.S. firms. TDP sponsored two such orientation visits by Turkish officials to expose them to American advanced education technology and introduce them to U.S. companies that can provide equipment or services in this sector. The visits were designed to address Turkish education needs financed by four World Bank loans. As a result of these visits, U.S. firms located in New Jersey, Massachusetts, and Ohio have already sold $28 million of equipment and services. Another $170 million in educational equipment, computer software, and consulting services are expected to flow from these "reverse trade missions."

In other instances, TDP has found that conferences and technology seminars serve to inform U.S. companies about export opportunities in a particular sector or region and/or to familiarize foreign officials with state-of-the-art U.S. technology. For example, TDP funded a feasibility study of a proposed transmission and substation project in Thailand. Following the study, TDP sponsored a business opportunities briefing to increase the awareness of U.S. manufacturers. Approximately $12 million of U.S. exports have already been generated from this project, and market opportunities exist for an additional $100 million.

Another important tool in strengthening economic opportunity for U.S. businesses overseas is state participation in TDP program activities. TDP has encouraged the states to participate in conferences and technology seminars where such involvement can enhance TDP's efforts and benefit state exports. For example, in November 1989, TDP funded the Conference on Asia-Pacific Petrochemical and Refinery Integration (CAPPRI) in Houston. CAPPRI was organized by the state of Texas, the East-West Center in Hawaii, and the University of Houston's Small Business Development Center. The purpose of CAPPRI was to bring together senior industry and government decision-makers from the U.S. and Asia to discuss regional petrochemical markets and development prospects for the 1990s. An integral feature of the conference was the opportunity for U.S. companies to learn about Asian oil and gas processing capability and to promote U.S. planning and technical services and products. CAPPRI opened an avenue for interregional exchange of information and trade between the U.S. and the Asia-Pacific in the energy and petrochemical fields. The potential investment opportunities identified during this conference have been estimated at $20-22 billion. TDP also works closely with state development agencies as a prime mechanism to disseminate information on export opportunities to U.S. firms.

TDP operates in most countries of the developing and middle-income world. Geographic responsibilities are handled by five regional officers. The regional officers travel to the countries assigned to them on the average of two to three times a year, depending on the level of activity in that country. The Department of Commerce's Foreign Commercial Service and other U.S. Embassy personnel play a critical role in providing support for the TDP program year round.

TDP considers each project proposal on its individual merits and does not pre-allocate resources by region. The actual funds obligated to projects in any region tend to reflect the demand generated by that region, the availability of financing for those countries, and the level of U.S. private sector interest in projects in those countries; thus regional concentration can be expected to shift somewhat from year to year.

In FY 1989, the countries receiving the largest amount of TDP funds were Bolivia, Venezuela, India, and Thailand. Obligations increased substantially in Latin America and Africa from FY 1988 to FY 1989 because of TDP's concentrated effort in these regions. In response to President Bush's initiatives in Poland and Hungary, TDP obligated $500,000 in Hungary in 1989, and is active in both countries. TDP participation in Eastern Europe is expected to expand significantly in FY 1990.

Eastern Europe:

TDP has established its role as a U.S. foreign assistance agency uniquely able to stimulate foreign economic development and exports of U.S. goods and services in a manner consistent with U.S. foreign policy goals and objectives. TDP's efficient response to urgent assistance requirements in the emerging democracies of Eastern Europe demonstrates the value of TDP in carrying out U.S. foreign policy initiatives.

Eastern Europe will be a primary focus for FY 1990 and FY 1991. TDP is actively pursuing opportunities in Poland and Hungary in response to the U.S. Government's initiative and the strong U.S. business interest in market opportunities in these countries. Six million dollars was authorized in the Support for Eastern European Democracy (SEED) Act of 1989 for projects in Poland and Hungary for fiscal years 1990-1992. TDP will provide funding for a minimum of $2 million each fiscal year for project planning activities in the following sectors: telecommunications, environmental protection, energy, transportation, and industrial and financial development. Eastern European officials have expressed a strong desire for U.S. goods and services.

TDP initiated its program in Hungary in July 1989 with a grant for $500,000 for a study of a project to down-size an inefficient metallurgical complex at Miskolc, Borsod County. The study, conducted by UEC, USX Engineers and Consultants, and the University of Pittsburgh, is currently underway.

TDP has focused its initial efforts with SEED funds in Poland and Hungary on the telecommunications sector. In Hungary, a grant for $500,000 to the Ministry of Transport, Communications and Construction is pending for a master plan for a new digital overlay network and for a technical orientation visit of Hungarian telecommunications officials to the U.S. In Poland, TDP plans to provide a grant of $700,000 to the Ministry of Communications for a planning study for modernization of the Polish telecommunications system. Both studies are anticipated to provide additional opportunities for exports of U.S. telecommunications goods and services, and they will provide the U.S. industry with valuable technical data as a basis for private sector proposals.

TDP has received additional requests for a study of electrical network distribution and control technology in Hungary and for a national air traffic control network in Poland for which definitional missions will be fielded to ascertain funding eligibility. Another definitional mission will focus on priority projects in the solid and hazardous waste sectors. Other areas of expressed interest which TDP will pursue, subject to the availability of funds, will include power sector modernization, transportation, and selected industrial priorities.

In regard to other Eastern European countries, TDP has had an ongoing program in Yugoslavia since 1985, and has funded a number of studies in that country, particularly in the energy and industrial sectors.

There is strong potential for TDP to do more work in such areas as health, computer technology, environmental, energy generation, telecommunications, pollution control, and alternative sources of energy.

Yugoslavia's business and foreign investment regulations are relatively liberal. Despite the country's economic difficulties, U.S. company interest in Yugoslavia has been strong for many years as a result of an aggressive private sector U.S.-Yugoslav Economic Council marketing Yugoslavia's commercial needs. TDP is eager to expand its programs in this country.

TDP is currently looking at Yugoslav project proposals in the energy and environmental sector. A TDP representative plans to visit Yugoslavia in May to identify project opportunities for possible U.S. company involvement.

TDP is aware of Yugoslavia's recent request for USG technical assistance and training in such areas as the development of capital markets, privatization, accounting standards, marketing and small business development. We currently are reviewing these proposals for possible TDP involvement.

While TDP has not as of yet initiated programs in Czechoslovakia, Romania or other Eastern European countries, their infrastructure requirements and priorities are similar. TDP is prepared to move quickly to develop programs to promote enhanced U.S. trade at such time as U.S. foreign policy permits.

Latin America and the Caribbean:

Latin America and the Caribbean offer vast potential markets for U.S. goods and services as economic growth returns to the region. In particular, with the new emphasis on opening of local markets and privatization of previously state-run sectors of the economy (telecommunications, power, railroads, etc), as well as the Andean Trade Initiative, there are growing opportunities for exports of U.S. goods and services, as well as U.S. investment. Therefore, TDP is giving increased attention to the Latin American region. This is reflected in the growth of TDP project funding from $1.7 million in FY 1987 to over $6 million in FY 1989.

In the past year, TDP has been especially active in Latin America, with a special focus on the Andean region, in line with the Administration's anti-drug strategy. TDP's project planning assistance on major projects helps the countries of this region develop their basic infrastructure and industrial base, which is essential for them to expand their trade and investment. For example, last year TDP funded a major $2 million minerals survey in Bolivia, which will help identify the best prospects for U.S. mining investments in that country. This in turn will create alternative employment opportunities for Bolivians now engaged in the drug trade. Similarly, in Venezuela, we have funded studies in the power, aluminum, and water sectors. In Ecuador, we expect to sign agreements soon for a major water project and a petroleum industry master plan. We are also looking at new projects in Colombia and are keeping abreast of developments in Peru.

TDP estimates that $2.3 billion of exports from U.S. companies will occur as a result of projects receiving initial funding from TDP in this region. The level of exports associated with TDP-funded projects will increase further as TDP activity in the region increases.

In addition, TDP is coordinating with overall U.S. Government efforts in Panama. TDP officials accompanied an OPIC investment mission to Panama and participated in several independent TDP working sessions with Panamanian officials during the week of February 24, 1990. During the trip TDP established a close relationship with leading members of the Panamanian cabinet and laid the foundation for a major TDP program in Panama.

Based on those meetings, the Vice Minister of Commerce and Industry has identified nine priority projects. In response, TDP has approved definitional missions to examine four of these potential projects. The projects could involve a TDP commitment in Panama of $1 to $1.5 million.

Asia:

TDP will continue to focus on the increasingly important industrial/economic sectors in Asia, such as telecommunications, energy, pollution control, and hazardous waste management. In FY 1989, approximately $8 million in grants were obligated in Asia. TDP is currently reviewing over $22 million of proposed projects for FY 1990 in this region.

TDP's program in Thailand has been and will continue to remain strong, especially as projects being presented to TDP for funding increase in size and complexity.

Because of the recent events in China, TDP has suspended all new activities in that country since June 1989. TDP activities in China have opened new long-term markets to U.S. firms and introduced U.S. technology and products to China. There has always been strong support from the business community for the China program and the commercial benefits it provides.

As of November 1989, $2.1 billion in exports from U.S. companies had gone to projects in the Asia region for which TDP provided planning activity funding. TDP projects an additional $13.4 billion in exports to those projects, for a total of $15.5 billion. Projects in five countries, China, Indonesia, the Philippines, Thailand, and Taiwan, have received 95 percent of the U.S. company exports in this region.

Africa:

The various African markets are difficult for U.S. companies to penetrate for economic and political reasons, but African countries are likely to yield significant future opportunities for U.S. exporters and investors. Thus, TDP support is important from a long-term strategic point of view.

TDP anticipates FY 1990 obligations in Africa of approximately $4.1 million, up from $2.5 million in FY 1989. TDP estimates that approximately $1.6 billion of U.S. exports will result in the long-term from projects associated with TDP planning activities financed through FY 1989 in this region.

During the next few years, TDP will focus its efforts on those African countries making significant progress in structural adjustment and economic reform. Such countries will provide more stable markets for U.S. companies. They are also the most likely to have multilateral funding for major development projects. While individual country development priorities are diverse, TDP anticipates an emphasis on agro-industrial development, telecommunications, mineral development, energy and transport.

TDP will actively pursue projects in Francophone Africa. These countries have made overtures in recent years which indicate a new interest in U.S. business relationships that TDP hopes to encourage.

Middle East and Europe:

TDP's activities in this region have included a variety of the major technological sectors including power, mineral development, telecommunications, agribusiness, transportation and educational technology. TDP anticipates that environmental technology will be a growing area in this region in coming years.

TDP estimates that approximately $2.3 billion in exports will be generated by projects associated with TDP-funded planning activities to date in this region.

Through FY 1988, TDP has obligated a total of $113 million for planning major projects. Although TDP grants are untied to follow-on procurement, almost $3 billion of U.S. exports have been associated with projects supported by TDP-funded studies to date. Moreover, these figures are only the tip of the iceberg. It can take many years to reap the benefits of investment from a feasibility study. The lead time necessary to move large-scale development projects to the implementation stage can run as long as ten to twenty years before final contract negotiations and financial backing are concluded. The bulk of equipment sales will usually come towards the end of a project's development. An independent analysis of exports associated with TDP-funded projects estimates follow-on exports of approximately $7-8 billion in the next ten years. This figure does not include exports indirectly attributable (second and third-generation equipment purchases) to TDP, and spin-off projects, which are difficult to document.

TDP's success is reflected not only in monetary terms. Its impact on Third World development, on helping U.S. firms to penetrate emerging markets, on building diplomatic and trade relations are all important results to be acknowledged as well.

TDP has devoted substantial efforts towards establishing high-level working relationships with ministry officials in its host countries. Our daily cooperation with the private sector, industry officials and other agencies, and our expertise in leveraging small amounts of funding to generate exports makes TDP a central player in the major project export market. U.S. companies who work with TDP have gained recognition and an opportunity to introduce U.S. equipment and technologies into new markets. In the international marketplace companies repeatedly receive offers and contracts for spin-off projects related to their participation on a TDP-funded project.

In this vein, while maintaining a broad program interest in all sectors, we have emphasized those where U.S. industry is strong (i.e., pollution control and hazardous waste in Asia and telecommunications in Latin America). Through the use of TDP funds in particular targeted sectors, market access can be achieved and U.S. exporters can obtain a market niche. A base is thus established for future market share against competitors from other industrial countries.

In closing, I would especially like to thank Mr. Obey and the members of this Subcommittee for their continued interest and enthusiastic support of TDP. We continue to appreciate the flexibility granted to TDP by the Congress, and intend to use that flexibility to work innovatively with the U.S. private sector, our trading partners, and other agencies of the States and the Federal Government to continue to promote U.S. trade in international development and cultivate free market principles in emerging economies. We believe we have a track record which speaks well for the mandate entrusted to us.

Mr. Obey. Thank you.

Mr. Berg.

Opening Statement of Mr. Berg

Mr. Berg. Thank you, Mr. Chairman. My name is James Berg and, as part of the Bush Administration's new management team at the Overseas Private Investment Corporation, it is an honor for me to appear before this subcommittee for the first time.

I take great pleasure in being here on behalf of OPIC to discuss with you the role of our finance program and related activities in strengthening U.S. economic opportunities.

These are truly exciting times for OPIC. As a government agency whose mission is to mobilize U.S. private investment for economic development, OPIC is poised to help promote American investment in countries that have recently undertaken significant political and economic reforms, as well as those more traditional beneficiaries of OPIC's programs.

Throughout Eastern Europe, for example, nation after nation is rapidly moving away from closed systems. In Panama and most recently Nicaragua, momentous changes have created unprecedented need for U.S. private sector investment as those countries begin the process of rebuilding their economies along free market lines. These and other events have opened up tremendous new demand for the services and programs that OPIC can provide.

To position OPIC to participate effectively in the face of the dramatic events currently unfolding, we have developed several new initiatives to complement our traditional and ongoing programs. These new endeavors, which are described in the written statement that I am providing today, are an integral part of our overall response to today's emerging development imperatives and to our strategy for the future.

Eastern Europe figures prominently in those new initiatives, and so do some new programs that we have developed for Africa, sub-Saharan Africa in particular.

I would like to take a brief moment and describe a recent investment mission that we had in Panama which was just mentioned by the previous speaker. We are playing an important and active role in the economic recovery initiative in that country.

OPIC IN PANAMA

To help rebuild the economy of Panama following the restoration of democratic government, we reopened our finance and political risk insurance programs as soon as the "Urgent Assistance for Democracy in Panama Act," P.L. 101-243, was signed by the President on Valentine's Day. Just nine days later, OPIC took an investment mission to Panama.

This was the first U.S. government-sponsored effort to bring American investors to Panama to begin the process of rebuilding that economy. Although Panama retained a relatively solid infrastructure of transportation, communications and electricity, key sectors such as agriculture, light industry and tourism urgently needed new capitalization and the infusion of new expertise.

Our mission included 27 U.S. private sector business executives. Mission participants were given an unprecedented opportunity to familiarize themselves with the economic and political climate in post-Noriega Panama through direct talks with government and business leaders.

By the end of the mission, participants had announced their intention to proceed with at least $70 million in new private American investment in projects in Panama, some of which will involve OPIC assistance in either the finance or the insurance areas, or perhaps both. These new investments we believe will generate more than 500 permanent new jobs in the 1990–1991 period.

OPIC PROGRAM

There are specific OPIC programs that are of interest to this committee, Mr. Chairman, and they are our finance programs, the direct investment fund loan program and our investment guarantee program. I will briefly outline the status of our request for those programs for this year, but let me begin by giving you a little bit of information about our equity program, which has been authorized, but to date which we have not had funding to implement.

The OPIC equity investment program was authorized by Congress as a four-year pilot program in 1988 to help facilitate private investment in two areas most in need of productive economic and social development projects, sub-Saharan Africa and the Caribbean Basin region.

The equity program was to be funded by a $10 million transfer from our reserves, and that was later made subject to advance approval in appropriation acts. The Administration's fiscal year 1990 budget request included a $3 million allocation to the equity program. That allocation was not included in the final appropriations act.

In fiscal year 1991, the Administration has requested authorization to expand eligibility of this program to provide much-needed seed capital for private investment projects in certain Eastern Europe countries as the President may designate. This particular request is contained in the Administration's proposed version of the so-called SEED–II Act.

For our finance program, the core of OPIC's finance program is our direct investment fund, which is reserved for projects sponsored by small and medium-sized companies, and our investment guarantee program, which is used for larger, capital intensive undertakings. Under these programs, OPIC provides loans and loan guarantees for new business ventures and expansions of existing projects sponsored by U.S. businesses in eligible developing countries.

Since OPIC's inception in 1971, nearly $1.6 billion has been committed for direct loans and investment guarantees to finance projects in 58 developing countries.

Each year for the past five years, OPIC has committed its entire lending authority as established by Congress. During fiscal year 1990, we again expect to commit the entire $19.9 million authorized for the direct loan program and the entire $211.5 million authorized for the investment guarantee program.

The fiscal year 1990 investment guarantee authority includes $39.3 million specifically authorized for projects in Poland, and we expect to commit that entire amount to support American private investment in that country.

Based on this successful record of use, the Administration has requested fiscal year 1991 funding levels of $23 million for OPIC's DIF program and $185 million for its IG program. These levels, which are consistent with amounts we have fully utilized in previous years, are essential to maintain our ongoing finance programs and to implement the numerous new initiatives that we have.

I will conclude there, Mr. Chairman, and would be pleased to answer any questions you might have.

[The prepared statement of Mr. Berg follows:]

STATEMENT OF

JAMES D. BERG

EXECUTIVE VICE PRESIDENT

OVERSEAS PRIVATE INVESTMENT CORPORATION

BEFORE THE

SUBCOMMITTEE ON FOREIGN OPERATIONS,
EXPORT FINANCING, AND RELATED PROGRAMS

COMMITTEE ON APPROPRIATIONS
U.S. HOUSE OF REPRESENTATIVES

March 21, 1990

Mr. Chairman and Members of the Subcommittee:

As part of the Bush Administration's new management team at the Overseas Private Investment Corporation, it is an honor for me to appear before this Subcommittee for the first time. I take great pleasure in being here on behalf of OPIC's President and Chief Executive Officer, Fred Zeder, to discuss with you the role of the finance program and related activities of OPIC in "Strengthening U.S. Economic Opportunities."

These are truly exciting times at OPIC. As a government agency whose mission is to mobilize private U.S. investment for economic development, OPIC is poised to help promote American investment in countries that have recently undertaken significant political and economic reforms, as well as those more traditional beneficiaries of our programs. In the year that has passed since our last appearance before this Subcommittee, remarkable political and economic changes have taken place worldwide. Throughout Eastern Europe, nation after nation is rapidly moving away from closed totalitarian systems, towards open, democratic societies and free market economies. In Panama and, most recently, Nicaragua, momentous changes have created unprecedented need for U.S. private sector investment as those countries begin the process of rebuilding their economies along new free market lines. These and other events have opened up tremendous new demand for the services that OPIC provides.

To position itself to participate effectively in the face of the dramatic events currently unfolding, OPIC has developed several new initiatives to complement its ongoing programs. These new endeavors, which are described later in my testimony, are an integral part of OPIC's overall response to today's emerging development imperatives.

I hope that my testimony today will serve two primary purposes. First, it should alert the Subcommittee to the new programs and initiatives being undertaken by OPIC to respond to the challenges of the quickly changing world. Second, I will review the status of our ongoing programs and describe OPIC's accomplishments during fiscal year 1989. For, as Fred Zeder has repeatedly emphasized, we do not wish our initiatives in Eastern Europe and Central America to overshadow or detract from our ongoing activities in other regions. Quoting from Mr. Zeder's introduction to OPIC's 1989 annual report: "The increased recognition, acceptance and demand for OPIC's products and services have created within our ranks a rededication and commitment to the programs we have been providing for nearly 20 years in developing countries around the world."

STATUS REPORT ON AREAS OF SPECIAL INTEREST

Eastern Europe

It is hardly necessary to mention that one of the most profound developments of 1989 was the movement throughout Eastern Europe away from communism and centrally planned economies, toward more democratic forms of government and free market principles. In the midst of these extraordinary events, OPIC was thrust into a highly visible and challenging new role.

Following the Administration's announcement in April 1989 of a new policy towards Eastern Europe, including an important role for OPIC there, and concurrent with legislation authorizing OPIC to open its programs in Poland and Hungary, we began active preparations to begin operations there. Bilateral agreements with both countries were signed, and in early November 1989 OPIC sponsored its first investment mission to Poland.

With participants from 29 U.S. companies, the Poland mission was the largest and most quickly organized in OPIC's history. Investor interest in Eastern Europe remains consistently high. To further promote private investment opportunities, OPIC will return to Eastern Europe later this spring with back-to-back missions scheduled for Hungary (April 22-27) and Poland (April 29-May 4). The main thrust of the mission will be to introduce U.S. business to specific joint venture opportunities and partners in the host nation. In addition to meetings with leaders in industry, commerce and government, the OPIC mission participants will be briefed on legal, accounting and banking practices and recent legislation affecting foreign investment and joint ventures in those two nations.

The economic development needs in Eastern Europe are extensive, ranging from agriculture to telecommunications and manufacturing. There is a particularly urgent need for environmental action, as East European nations strive to mitigate air, soil and water pollution. An underlying need, common to all sectors of these newly emerging market-based economies, is for the transfer of technological, operational and management skills to local enterprises as they are transformed from centralized to private entities.

In January 1990, OPIC approved its first project in Eastern Europe. OPIC issued an insurance contract covering General Electric Company's $150 million investment in Hungary to acquire a majority interest in Tungsram, an electric lighting products manufacturer. OPIC insurance was a key element in this venture to protect against uncertainties in the transition from a planned economy to a market economy. Based on preliminary project registrations, investor inquiries, and the level of interest in the upcoming OPIC missions, OPIC expects to support numerous additional investments in Hungary and Poland in the coming months.

As you know, OPIC programs may soon be extended to other countries in Eastern Europe. Under the proposed Eastern European Democracy and Free Market Act of 1990, OPIC would be authorized, if conditions warrant, to begin operations in Czechoslovakia, the German Democratic Republic, Romania and Bulgaria. This important legislation builds on the steps previously taken to respond to the economic, political and social revolution currently underway in Eastern Europe.

As part of expanding its programs into Eastern Europe, OPIC has sought to promote continued progress with regard to internationally-recognized workers rights. In this connection, OPIC has consulted with U.S. labor organizations, including the AFL-CIO, regarding measures to ensure that OPIC's economic development activities promote respect for worker rights. OPIC has agreed with the AFL-CIO to incorporate in OPIC's insurance contracts in Poland and Hungary language to ensure that investors receiving OPIC political risk insurance coverage respect internationally recognized worker rights. This measure reinforces worker rights provisions already included in OPIC's statute.

We look forward to additional cooperation and consultation with U.S. labor organizations in monitoring labor conditions throughout Eastern Europe. OPIC's activities are aimed at promoting respect for the rights of the very men and women whose courage and determination set into motion the historic reform process which is transforming the world.

Panama

OPIC is playing an active and important role in the economic recovery initiative in Panama. To help rebuild the economy of that country following the restoration of democratic government, OPIC reopened its finance and political risk insurance programs as soon as "The Urgent Assistance for Democracy in Panama Act of 1990", P.L. 101-243, was signed by President Bush on February 14, 1990. On February 23, 1990, OPIC took an investment mission to Panama. This was the first U.S. Government-sponsored effort to bring American investors to Panama to begin the process of rebuilding its economy. Although Panama has retained a relatively solid infrastructure of transportation, communications and electricity, key sectors such as agriculture, light industry and tourism urgently need new capital and expertise.

The highly successful OPIC mission included 27 U.S. private sector business executives. Mission participants were given an unprecedented opportunity to familiarize themselves with the economic and political climate of post-Noriega Panama, through direct talks with government and business leaders. By the end of the mission, participants had announced their intention to proceed with at least $70 million in investment projects in Panama, some of which may involve OPIC assistance, finance and/or insurance. These investments are expected to generate more then 500 permanent jobs during 1990-1991.

Ireland/Northern Ireland

Because of the tremendous need for economic revitalization in both the Republic of Ireland and Northern Ireland, OPIC programs are available there to identify, develop and support eligible projects which could benefit from U.S. investment. Underscoring our commitment to this area, OPIC's President visited Northern Ireland in the summer of 1989.

In one particularly promising project OPIC is currently working closely with the Industrial Development Board for Northern Ireland in support of U.S. investment in and refurbishing of a manufacturer of jute and wool processing machinery in West Belfast. The project, which received host government approval in January 1990, will secure employment for more than 600 workers in this area, where the unemployment rate currently stands at 45%.

Africa

To focus on the particular needs of African economies, OPIC continues to develop new capital formation techniques targeting this region.

For example, in coordination with the Agency for International Development ("AID"), OPIC is laying the groundwork for the establishment of privately owned or operated export processing zones in the sub-Saharan countries of Togo and Cameroon. Export processing zones are areas designated by host governments to provide tax incentives and other benefits to export manufacturers. After conducting preliminary research, OPIC concluded that supporting the establishment of privately operated zones of this kind in sub-Saharan Africa might be an effective way to encourage additional investment in manufacturing, both foreign and indigenous. Following a more detailed study of Togo and Cameroon, OPIC and AID concluded that excellent potential for such zones exists in both countries, and pre-feasibility studies are currently underway. The OPIC finance program expects to be involved in supporting eligible U.S. businesses operating in the free zones. An OPIC investment mission to this part of Africa is scheduled for September.

With respect to a second OPIC initiative targeting Africa, and one that is already familiar to this Subcommittee, I am pleased to inform you that the Africa Growth Fund ("the Fund") was formally established in September 1989 as a privately owned and privately funded investment company that invests in new and expanding private sector enterprises throughout sub-Saharan Africa. The Fund is a limited partnership with total capitol of $10 million in private equity and $20 million in OPIC-guaranteed long-term notes.

The Fund is managed by Equator Investment Services Limited, a subsidiary of Equator Bank. Under the direction of its owners' committee, the Fund is presently reviewing numerous investment proposals identified during recent months. Opportunities for investment exist in the manufacturing, agricultural, finance and service industry sectors. The Fund is working closely with other major international development agencies which are expected to refer projects to the Fund and provide co-investment support for Fund projects.

Incidentally, the Government of Zimbabwe has announced it will sign shortly the OPIC bilateral agreement which was negotiated last summer, thereby adding a new country in which OPIC and the Fund will be permitted to operate. This is the culmination of many years of effort and is indicative of Zimbabwe's more positive recent attitude toward foreign investment and private enterprise.

In North Africa, OPIC's President led an investment mission to Morocco in November 1989. Recent changes in the investment laws of that country will facilitate foreign investment in development projects, where urgent need exists in the areas of agribusiness, food processing, manufacturing and energy. We also negotiated a bilateral agreement with Algeria which is currently awaiting signature, and which will allow us to bring our programs to that country too.

Finally, OPIC's ongoing efforts to increase U.S. investor interest in sub-Saharan Africa yielded two notable financings in 1989. One, a $3.4 million loan guaranty, will help an Oregon firm carry out a long-term contract with the World Health Organization to spray aerially for "river blindness" disease in 11 West African nations. The second, a $1 million loan for a brick and tile manufacturing plant in Botswana, stemmed directly from OPIC's investment mission to the Southern Africa region in the spring of 1989.

China

Unforeseen international events have also affected OPIC programs in less positive ways than have the changes in Eastern Europe. In June 1989, OPIC stopped assisting new projects in China pending determination of human rights and other conditions in China following the tragic events of Tiananmen Square. The Foreign Relations Authorization Act for Fiscal Years 1990 and 1991 placed specific restrictions on OPIC programs in China, and we are, like all of you, watching developments in China very closely.

Equity Program

The OPIC Equity Investment Program was authorized by Congress as a four-year pilot program in 1988 to help facilitate private investment in two areas most in need of productive economic and social development projects, sub-Saharan Africa and the Caribbean Basin. The program was to be funded by a $10 million transfer from OPIC's income and revenues, later made subject to advance approval in appropriations acts.

The Administration's FY 1990 budget request included a $3 million allocation to the equity program, which was not included in the final appropriations act. In FY 1991, the Administration has requested authorization to expand eligibility of this program to provide much needed seed capital for private investment projects in certain Eastern European countries as the President may designate.

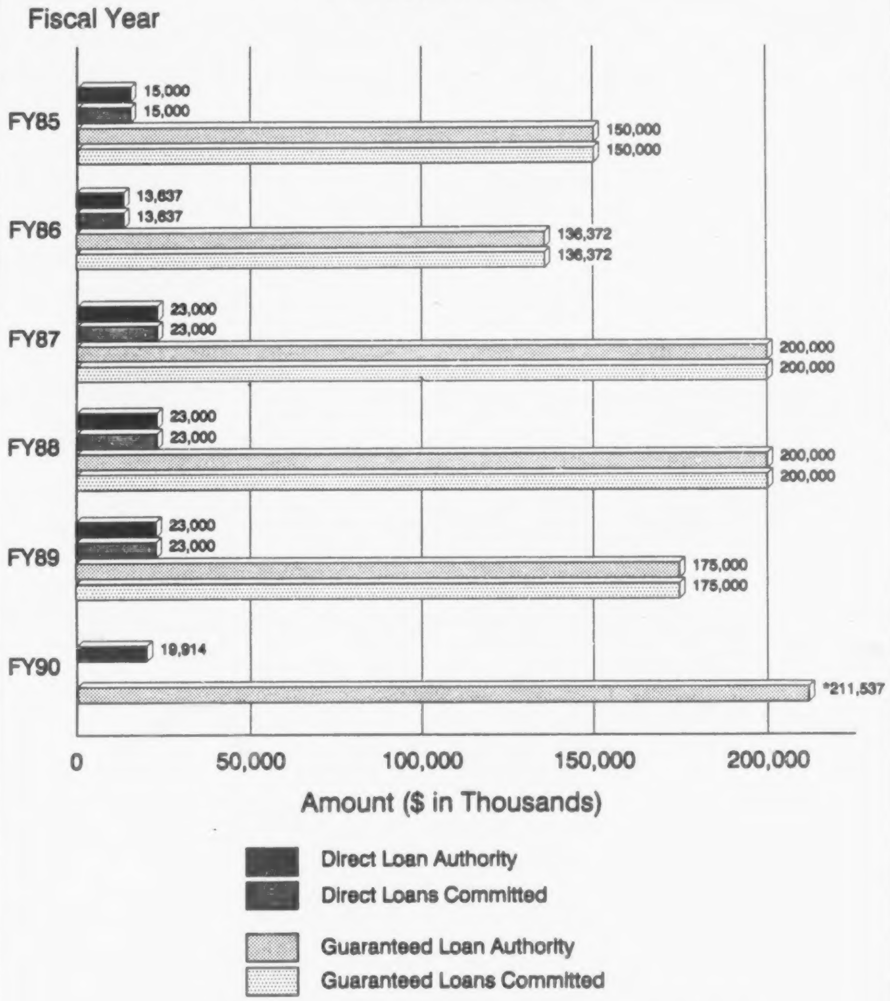
OPIC FINANCE PROGRAM

The core of OPIC's finance program is its Direct Investment Fund ("DIF"), which is reserved for projects sponsored by small and medium-sized companies, and the Investment Guaranty ("IG") program, which is used for large, capital-intensive undertakings. Under these programs, OPIC provides loans and loan guaranties for new business ventures and expansions of existing projects sponsored by U.S. businesses in eligible Third World countries. Since OPIC's inception in 1971, nearly $1.6 billion has been committed for direct loans and investment guaranties to finance projects in 58 developing countries.

Each year for the past five years, OPIC has committed its entire lending authority as established by Congress. During FY 1990 we again expect to commit the entire $19.9 million authorized for the direct loan program and $211.5 million of investment guaranty authority. The FY 1990 IG authority includes $39.3 million specifically authorized for projects in Poland, and we expect to commit that entire amount for that purpose. Chart 1 on the following page illustrates OPIC's utilization of its lending authority during the period FY 1985-FY 1990.

CHART 1

OPIC FINANCE PROGRAM
Utilization of Lending Authority as Approved by Congress
FY 1985 - FY 1990



*Includes $39,356,000 in guaranty authority earmarked for Poland.

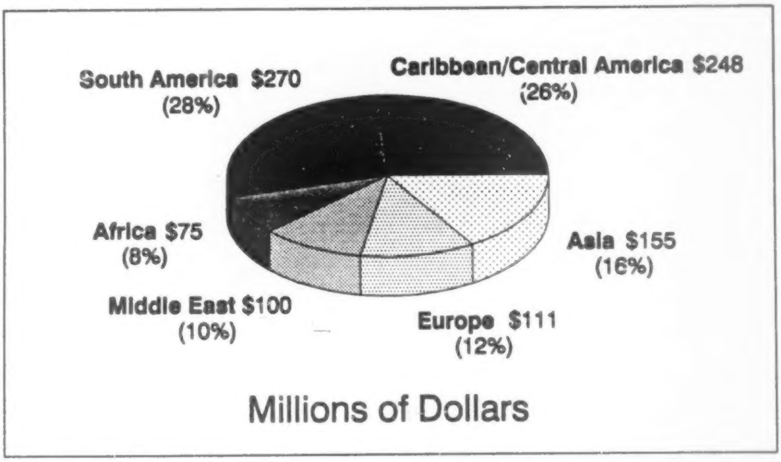
Based on this successful track record, the Administration has requested FY 1991 funding levels of $23 million for OPIC's DIF program, and $185 million for its IG program. These levels, which are consistent with amounts we have fully utilized in previous years, are essential to maintain our ongoing finance programs, and to implement the numerous new initiatives which I will describe later on.

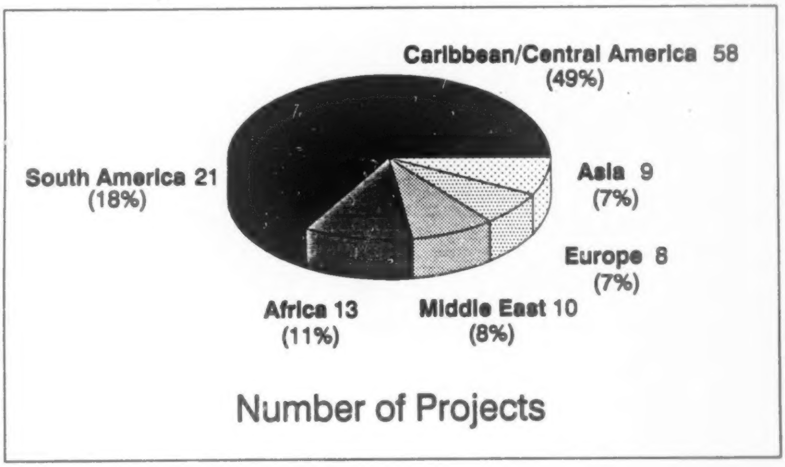
Review of FY 1989 Finance Program Accomplishments

Fiscal 1989 proved exceptionally productive for OPIC's finance program, which assisted 21 projects in 13 developing countries and areas. Over 70% of the year's projects were located in the world's poorest developing nations, as measured by per-capita GNP levels. Geographically, the year's projects were distributed as follows: 52% were located in the Caribbean Basin/Central American region; 19% were located in South America; 10% were located in Africa; 9% were located in Europe (Turkey); and 5% were evenly distributed between the Middle East and Asia.

Historically, OPIC finance projects have had a broad geographic distribution throughout the developing world. Chart 2 on the following page illustrates the regional distribution of OPIC finance projects during the period FY 1985 through FY 1989.

CHART 2
OPIC FINANCE PROGRAM
Geographic Distribution of Projects
FY 1985 - FY 1989





Host Country Developmental Effects of FY 1989 Projects

The 21 finance projects committed by OPIC in FY 1989 will generate significant economic and social benefits in their host countries. Notably, the net foreign exchange benefits to developing countries from the year's projects are projected to total $284 million per year. Other favorable impacts include initial expenditures of more than $571 million for local procurement of goods and services, employment of more than 5,900 local workers by the fifth year of project operations, and generation of $65 million in annual host government revenues.

Such benefits to the host country are best illustrated by the following two examples of FY 1989 finance projects:

Project: Aerial spraying to control "river blindness"

Region: West Africa

As mentioned previously, a $3.4 million OPIC loan guaranty will help an Oregon firm carry out a long-term World Health Organization ("WHO") contract to provide aerial spraying services to control the spread of a disease known as onchocerciasis. Often referred to as "river blindness," the parasitic disease affects 20 to 30 million people worldwide. It is particularly common in West Africa, where it is transmitted to humans through several blackfly species which breed in rivers and streams.

The onchocerciasis control program is recognized as one of the most successful programs of its type in the world. Eradication of this disease will enable the population to re-inhabit and cultivate fertile river bottomlands.

WHO's satisfaction with the project sponsor's performance on a previous contract, which was also supported by OPIC, helped secure the present contract, which runs through December 31, 1992, and involves spraying operations in eleven countries: Benin, Burkina Faso, Cote d'Ivoire, Ghana, Guinea, Guinea Bissau, Mali, Niger, Senegal, Sierra Leone, and Togo.

Project: Reconstruction and expansion of poultry farms

Country: Jamaica

Through a direct loan of $3 million, OPIC is assisting in the reconstruction and expansion of several poultry farms destroyed by Hurricane Gilbert in 1988. The project stems from a special OPIC "rehabilitation" mission undertaken in November 1988 to expedite the recovery of Jamaica's private sector economy in the wake of the hurricane's destruction.

In addition to the reconstruction of the farms, the project involves the upgrade and expansion of a related broiler processing facility.

Employing over 1400 Jamaicans, the project company is the leading firm in the country's poultry business. This project will safeguard these jobs, and the expanded operations will provide an additional 83 new jobs.

Chart 3 on the following page illustrates the cumulative host country developmental benefits for all OPIC direct loan and investment guaranty projects committed during the five-year period from FY 1985 through FY 1989.

CHART 3

OPIC FINANCE PROGRAM
Estimated Developmental Impact of Projects
FY 1985 - FY 1989

Annual Foreign Exchange Effects For Host Country *	Amount/Number (millions of $, or number of workers)
Foreign Exchange Benefits	
Imports Replaced	$ 861
Exports Generated	2,099
Total	$ 2,960
Foreign Exchange Costs	
Project Imports	$ 679
Capital Outflows	1,319
Total	$ 1,998
Net Foreign Exchange Benefit (Benefits - Costs)	$ 962
Net Annual Taxes, Revenues and Duties Paid to the Host Country*	$ 613
Initial Local Expenditures	$ 1,603
Local Employment Generated**	
Technical and Management	4,326
Skilled and Unskilled Labor	24,617
Total	28,943

* Average annual amount over a five-year period.
** Number of workers in fifth year of operation.

U.S. Economic Effects of FY 1989 Projects

The 21 finance projects committed by OPIC in FY 1989 will also have a favorable impact on the U.S. economy. In addition to the $684 million of total U.S. investment in the projects, initial exports of U.S. machinery, equipment and supplies are valued at $412 million, while operational procurement from U.S. sources will generate an additional $765 million during the first five years of project operations.

The U.S. exports generated by these projects will result in the creation of an estimated 7,000 person-years of U.S. employment. The net direct U.S. trade effect of these 1989 projects will amount to a positive $620 million contribution toward the U.S. balance of trade and, when all financial flows are considered, a net positive $693 million contribution to the U.S. balance of payments.

Twelve projects, or 57% of the year's total, involved significant participation by U.S. small business and cooperatives, defined as industrial companies with annual sales of less than $142 million and non-industrial companies with stockholders' equity of less than $48 million.

The following two examples of finance projects committed during FY 1989 illustrate the U.S. effects of our loan and guaranty projects:

Project: Construction of international airport terminal

Country: Turkey

OPIC issued a commitment for a $40 million OPIC loan guaranty to help finance the construction of a new international terminal at Istanbul's Ataturk Airport, and the conversion of the existing facility into a new domestic terminal. In all, the expansion will more than double the airport's aircraft, passenger and cargo handling facilities.

The ownership structure of the project, which brings majority U.S. ownership to a venture traditionally handled by the public sector, was made possible by a new Turkish government policy encouraging privatization.

Goods and services valued at $60 million will be purchased from the U.S. These purchases include the jetways, baggage handling equipment, prefabrication of a large atrium, other specialized construction materials, and engineering and design services. Cash flows arising from the operating contract amount to an average $2.2 million per year in ongoing U.S. procurement. Over the first five years of operation, the project will generate positive U.S. balance of payments effects of $69 million.

Project: Expansion of a winter melon production facility

Country: Guatemala

On a much smaller scale than the project cited above, an OPIC loan of $1.5 million will support the expansion of a winter fruit and vegetable growing and packing operation in western Guatemala.

The project sponsor, a small, family-owned Florida business, has been actively involved in the production and import of winter fruits and vegetables for over fourteen years. The company is the largest independent U.S. importer of fresh fruits and vegetables from Central America and the Caribbean.

Highlighting the "pioneering" aspect of this project is the fact that the sponsor is introducing a new cash crop to the Guatemalan farmers as an alternative to illicit crops such as coca and marijuana. In addition, the company works hard to support and service its growing number of independent growers.

A "hands-on" manager, the U.S. sponsor maintains extremely high production and quality standards for the project. A qualified U.S. technical staff of experts in soil analysis, plant disease, and insect control provides strict production guidelines. All of the company's technical breakthroughs, from fertilizers and pesticides to irrigation and quality control techniques, are passed on to its growers.

The project helps to fill the seasonal gap in the supply of melons for the U.S. market. This shortage, which exists annually from November to April, occurs when U.S. suppliers cease production in late fall.

Last year, the project sponsor imported more than 1,000 containers of produce into the United States, supporting over 400 U.S. wholesalers and distributors. Indirectly, employment was maintained along the entire shipping, distribution and retail chain during a time when seasonal lay-offs are customary.

Chart 4 on the following page indicates the cumulative U.S. effects of all OPIC direct loan and investment guaranty projects during the five-year period from FY 1985 through FY 1989.

CHART 4

CPIC FINANCE PROGRAM
Estimated U.S. Economic Benefits of Projects
FY 1985 - FY 1989

Total Project Investment	$ 5.5 billion
U.S. Investment in Projects	$ 2.7 billion
U.S. Percent of Total	49 percent
Total Direct U.S. Project Exports	$ 3.4 billion
Initial Procurement From U.S.	$ 1.4 billion
Operational Procurement (5 Years)	$ 2.0 billion
Estimated U.S. Employment Generated	23,030 person-years

NEW INITIATIVES

In addition to its traditional direct loan and investment guaranty programs, OPIC is developing several new initiatives corresponding to current global economic and environmental priorities. Specific new programs are described below. Others, yet in the preliminary "drawing board" stage of development, will target Asia and Central America.

Eastern European Growth Fund

One investment vehicle being developed by OPIC in response to the rapidly changing events in Central Europe and Eastern Europe is the Eastern European Growth Fund, which is designed to raise private capital to fund new business enterprises. This fund will have a target capitalization of $200 million, of which OPIC's participation will be approximately 25%. It will generate vital new economic activity in Eastern Europe by encouraging private sector growth.

The Eastern European Growth Fund will mobilize additional capital to address the excess demand for OPIC-type finance services in Eastern Europe. Requests for OPIC's support in the area of privatization alone could reach several hundred million dollars in the next year or two, and can be targeted at projects and sectors which may not be served by other investment fund initiatives.

Small Business Loan Guaranty Program for Poland

A second OPIC initiative targeting Eastern Europe, the Small Business Loan Guaranty Program for Poland, will provide loans of up to $500,000 to investment projects sponsored by U.S. small business investors. Eligible projects will include new ventures or the expansion of existing businesses, and may either be wholly-owned by U.S. companies or joint ventures between U.S. and Polish firms.

This facility is being undertaken to meet the strong demand in the U.S. small business community for OPIC financial support to develop investment opportunities in Poland. Through this "multiplier" program, OPIC will seek to establish working relationships with commercial banks in key regions of the United States to facilitate U.S. small business investment in Poland.

Environmental Investment Fund

OPIC places a very high priority on protection of the environment. To facilitate private investment in projects that can develop natural resources on a sustainable basis, without industrial pollution, OPIC is developing an Environmental Investment Fund, with support from the Agency for International Development, potential investors, and other interested agencies, foundations and corporations. This will be a privately owned and managed fund of up to $100 million (with 50% OPIC participation), which will identify, invest in, and support new or expanding business enterprises in developing countries which use natural resources on a sustainable basis and otherwise practice sound environmental management. OPIC proposes that this fund invest in equity securities of project companies whose businesses are in one of four broadly defined sectors: sustainable agriculture, forest management, ecotourism, and pollution prevention.

In preparation for launching the fund, OPIC has completed project profiles of the kinds of projects the fund might consider for investment, and prepared a concept paper on the fund's structure, capital base, management and investment strategy. We are currently developing procedures to identify potential financial advisors and placement agents for the fund as well as a qualified firm to manage the fund on a day-to-day basis.

The establishment of this fund is a high priority for OPIC. We currently expect to present this environmental fund for approval at OPIC's next Board of Directors meeting.

The Finance Program as a Government Credit Program

The management of OPIC's Finance programs fully meets the objectives of the Federal Managers' Financial Integrity Act

(FMFIA) and related requirements and guidelines. In addition, during FY 1989 OPIC implemented several changes to further strengthen its financial management systems and internal controls.

With respect to the Finance program, specific steps taken include the establishment of an independent credit analysis group within the Finance department to review prospective loans; the establishment of a separate credit review function in the Treasurer's office to review the loan portfolio following disbursement; the implementation of a pre-disbursement and post-disbursement loan rating system; and the development of more formal internal credit procedures.

In light of our rapidly growing business activities, OPIC recently re-evaluated its accounting policies with respect to its contingent liabilities and related reserves. Based on this review, OPIC elected to establish two new non-specific reserves. After careful analysis of the finance and insurance portfolios and OPIC's loss experience, in FY 1989 a $16 million reserve was created for investment guaranties, and a $34 million reserve was established for political risk insurance, in addition to our combined statutory reserves of $1.4 billion.

This new accounting policy is an important step in ensuring the continued sound growth of OPIC operations in the developing world. As our portfolio continues to grow as we implement new initiatives and as political and economic conditions evolve worldwide, OPIC will reassess these reserves annually, and increase them as necessary to maintain prudent levels.

It should also be noted that since its inception, the net actual losses under OPIC's investment guaranty program have represented only 3.7% of the total contingent liabilities created. Based on this strong historical performance, coupled with the recent and ongoing efforts to strengthen our financial management and controls as discussed above, OPIC believes that the investment guaranty program is not likely to result in any significant net actual losses (or outlays) in the future.

CONCLUSION

Commercial bank retrenchment from Third World investment, coupled with a heightened awareness of the importance of private sector investment as an alternative to public sector spending, underscore the importance of the OPIC finance program to strengthening U.S. economic opportunities in today's global market. OPIC will continue to develop innovative approaches to fulfilling our statutory mandate to mobilize the private sector in support of our national policy goals, and to use the finance authority made available to promote economically, politically and environmentally sound development worldwide.

Thank you, Mr. Chairman. I would be pleased to respond to your questions.

Mr. OBEY. Thank you.

Let me suggest we suspend temporarily so we can answer one of these wonderful roll calls we have on the floor. We will be right back.

[Recess.]

Mr. OBEY. Mr. Brown.

OPENING STATEMENT OF MR. BROWN

Mr. BROWN. Mr. Chairman, members of the subcommittee: I also welcome the opportunity to meet you and the members. I have a particular interest in this topic. I believe that U.S. economic assistance must become part of the U.S. effort to compete in the global market. Our competitors successfully use their aid programs for that purpose. That is what about 80 percent of the Japanese aid program goes for. In fact, every donor except the United States concentrates a major portion of their aid money on commercial objectives.

More generally, I agree with the common theme that you have expressed here, and that is that it is time to think about changing or responding to change. Some of the important factors we must address include the following three: First, many aid recipient countries would prefer assistance in the form of capital equipment and high-tech technical assistance. This is particular true for the more advanced developing countries, which are important commercially and in terms of the aid budget.

Second, is the obvious success of other donors in combining successful development with commercial advantage. I believe we have much to learn from the Japanese and the others.

Third, is the changing global context for U.S. aid. Declining Cold War tensions probably mean that economic competition should be a higher priority for aid.

Let me try to present some points about tied aid and mixed credits, items that are of interest to this committee. Mixed credits, as you well know, are a specific type of aid where export credit money is blended with aid. Since the early 1980s, the United States government has attempted to reach agreement among all donors to end the practice of mixed credits. This effort continues under the Bush Administration.

Nevertheless, at this time we must note that our competitors have increased their use of mixed credits almost fourfold since the early 1980s. A recent study done by CSIS estimated that U.S. exporters lost $5 billion of business annually due to mixed credit offers that the United States was unable to match.

The whole of the Japanese overseas economic cooperation fund, their program, is the equivalent of a mixed credit program, as its terms are less than 50 percent grant. It remains tied to Japanese exports.

AID and the Eximbank are looking at new ways to collaborate using war chest moneys to achieve good development. This effort is based on an agreement that AID will be involved only in projects that make sound development sense. One of the advantages of this strategy from our perspective is that it leverages AID funds for key projects.

We are also cooperating with OPIC, TDP in the pursuit of our mutual objectives. In my opinion, U.S. capital goods and exports will be essential to growth throughout the developing world. AID's experience shows that promoting U.S. economic interests could well improve development impact. More specifically, we can emphasize U.S. technology without affecting negatively the development impact.

At the same time, AID's primary mission is not export promotion. We remain a development institution. We will also be involved in a wide variety of countries, each of whose requirements will vary. In many of these countries, mutual benefit programs that involve direct benefits to U.S. businesses will probably remain very small.

AID has many different objectives and economic self-interest will not loom large everywhere. However, in some places economic self-interest is likely to produce a better development impact. Early aid successes in Western Europe and in the Far East were predicated on such an approach.

We have long recognized that assistance should be seen as a transitory bridge to sustainable trade and private investment flows. Using AID resources to build that bridge should be key to our program in the more advanced LDCs.

Because our resources are limited and we must meet competing objectives, AID will have to leverage any resources devoted to mutual benefit. Wherever possible, we will have to rely on capital project funding available from the multilateral banks and, even more important, from U.S. business and the U.S. private capital market.

The bottom line is that we can do more in many countries. To be effective, AID will have to collaborate with others in the U.S. government and outside of the U.S. government. We will also have to remain committed to sound development projects and strategies, an approach which I believe also makes good business sense. And we will have to recognize the competitive realities of the 1990s, realities that include tremendous opportunities in many parts of the developing world, as well as competitors who have done better at linking their development assistance to their own economic self-interest.

Thank you very much, Mr. Chairman.

[The prepared statement of Mr. Brown follows:]

(EMBARGOED UNTIL DELIVERY, MARCH 21 AT 10:00 AM)

STATEMENT OF
REGINALD J. BROWN
ASSISTANT ADMINISTRATOR FOR
PROGRAM AND POLICY COORDINATION
BEFORE THE
HOUSE FOREIGN OPERATIONS SUBCOMMITTEE

MARCH 21, 1990

Mr. Chairman, Members of the Subcommittee:

I am pleased to be here this morning to review with you the Bush Administration's views on "Strengthening U.S. Economic Opportunities" and foreign assistance.

This is my first appearance before this committee and I welcome the opportunity to get to know you Mr. Chairman and the Members of the Subcommittee to develop a relationship for future consultations on foreign assistance.

Three weeks ago Secretary Baker testified before your committee that we are facing a world in transition -- a world that can be shaped by basic American values such as freedom, democracy, human dignity, and fair play. The changing circumstances in Eastern Europe with communism being replaced by free market economic systems is just one example.

But our challenge is not just to take on the new economic assistance clients in Eastern Europe and Central America. Our aid program is also part of the U.S. response to changing economic interests around the world every bit as profound as the new political realities of Eastern Europe or Central America.

The simple fact is that U.S. economic assistance must be seen as part of our effort to compete in the global market in addition to serving any humanitarian and political interests. Our trade competitors use aid programs to promote economic interests. That is what well over half of the Japanese aid program goes for. In fact, every donor except the U.S. concentrates a major part of their aid money on commercial objectives. Not coincidentally the countries that other donors focus significant portions of their aid programs on are the high growth developing country markets.

Another way to consider the link between current A.I.D. programs and U.S. exports is to consider the country allocation priorities. The top five developing country importers of U.S. capital goods (in 1988 received less than 1% of total economic assistance (versus 24% of total aid in 1962). For Japan, their top five developing country markets (Korea, China, Thailand, Malaysia, Indonesia) received 30 percent of their aid in 1988. Trade also directly connects U.S. economic fortunes to developing countries.

The most important contribution the U.S. makes to economic progress in developing countries is its own growth. U.S. economic growth has generated increased markets for developing country exports and in turn the fastest growing developing countries have proven to be the best markets for U.S. exports.

At the outset let me emphasize that economic, humanitarian and strategic considerations are compatible. Promoting broad-based growth and social progress will remain paramount even where the link to U.S. economic self-interest is remote. Similarly, other special concerns like environmental sustainability -- which affects all of us -- must be addressed. But we also believe that promoting U.S. economic interests is possible even within existing budget constraints, political priorities and pressing new objectives for aid programs.

A.I.D.'s efforts in this regard are part of the overall Bush Administration strategy for international economic leadership. Our part is outlined in the Economic Policy Council's (EPC) paper sent to Congress in early September 1989. It outlines the Administration's commitment to help U.S. businesses compete on a "level playing field." As part of this overall effort, A.I.D. was directed to consider how we might reorient U.S. foreign assistance programs to help level the playing field. We were particularly asked whether more could be done within existing budgets to promote trade and investment. We are now completing our work on this initiative and hope to be able to share this with you soon.

Beyond the EPC concern about U.S. competitiveness, a range of new factors suggests that it is time to rethink current economic assistance priorities:

First there is the growing evidence that some aid recipient countries would prefer assistance in the form of capital equipment and "high-tech" technical assistance. This is particularly true for the more advanced developing countries which are important commercial partners of the U.S. and who receive a major portion of the aid budget.

Second is the obvious success of other donor claims for their programs in combining successful development with promoting commercial advantage. This is where other donor models of flexible country programming and greater reliance on the private sector are particularly important. I particularly believe, even as the Japanese can learn from us, we have much to learn from the Japanese.

Third is the changing global context for U.S. aid which reflects decreasing Cold War tensions even as concern about economic competitiveness mounts.

The competitive threat of some other donor assistance programs is often pointed to because of their growing size and their explicit link to trade. For example, over 80% of Japan's high technology exports to high-growth developing countries in the Pacific Rim are financed through its aid program while U.S. assistance has done little in these sectors in these countries.

Despite the commercial emphasis of other donor programs and the lack of such emphasis in our program, the U.S. share of the market for LDC imports of capital goods has continued its historic upward trend. Although the LDC market is less important to the U.S. than it once was (in the 1960s, over half of all U.S. capital goods exports went to LDCs; today about 20%), our share of the market for LDC imports of capital goods has increased from 22.4% in 1979 to 33.8% in 1988. This is a testimonial to the popularity of U.S. products and the continuing "comparative advantage" of the U.S. in many LDCs.

However, the importance of LDC markets and the U.S. ability to compete in them could change dramatically in the coming decade. New challenges and opportunities exist in:

- The untapped potential of Eastern Europe which is the size of the Latin American economy
- Other donor initiatives to exploit export opportunities to developing countries and Eastern Europe.
- Japan's capital surplus and its effects on direct investment, trade and aid.

A.I.D.'s Current Operations and Exports

A.I.D. does not collect detailed information about the link between development assistance and exports of goods and services.

Experience probably varies greatly from country to country and reflects various factors such as recipient country needs and U.S. competitiveness in particular markets or products.

It is also worth emphasizing that the functional account definitions and earmarking severely limit our ability to use DA resources for "mutual benefit" programs in more advanced developing countries. Even where recipient government priorities and social needs suggest attention to technology gaps or infrastructure, the DA account definitions inhibit effectiveness. For example, it is impossible to finance productive infrastructure using DA in some countries even when the benefits would go to the poor.

Some forms of Economic Support Funds or ESF remain tied to U.S. exports. About 40% of total ESF is tied to U.S. exports through commodity import programs or projects where "Buy American" requirements are applied. Projectized ESF is, in fact, where the bulk of A.I.D.'s current infrastructure project and capital equipment financing takes place.

Our food aid remains purely tied to U.S. exports. While often criticized as less effective than cash grants, food aid is politically popular in the U.S. because it benefits U.S. farmers. I believe there's an important lesson for those of us concerned about the support for foreign aid.

Highlights

Some country highlights of current A.I.D. efforts to promote capital exports through infrastructure projects include the following:

- Large Economic Support Fund programs like Egypt. Bipartisan Congressional support for "projectizing" Economic Support Funds has enabled A.I.D. to run a large capital projects program in countries like Egypt. A good project example is the Shoubra El Kheima Power Plant where A.I.D. provided $266 million of the total $750 million project cost. The plant was completed ahead of schedule and under-budget, and resulted in over $500 million of U.S. exports.

- Feasibility studies that lead to U.S. exports. In the Philippines resources provided by the Multilateral Assistance Initiative have been used to create a $25 million fund to finance feasibility studies by U.S. or local consultancy firms for capital projects that would involve substantial U.S. exports.

- Transportation infrastructure in Africa. A.I.D. is involved in a number of transportation infrastructure projects in Africa that involve capital equipment. As part of the efforts to help countries bordering South Africa, A.I.D. has obligated over $150 million for railways and roads through this fiscal year. For example, for the Tanzania-Zambia railway A.I.D. is funding $40 million of U.S. railway equipment.

- Trade financing in Central America and Eastern Europe. A.I.D. collaborates with the Eximbank by providing guarantees to facilitate trade credit for American origin exports to Central America. To date the Trade Credit Insurance Program or TCIP has helped finance $700 million in U.S. exports to Central America because of A.I.D.'s guarantees. A similar $200 million TCIP program has been mandated by Congress for Eastern Europe and is being implemented.

TIED AID, AND MIXED CREDITS

We need to clarify some definitions of "tied aid" and "mixed credits" for the record. I believe there is a great deal of confusion surrounding these terms and how A.I.D. employs both tied aid and mixed credits.

Tied Aid

Tied aid simply means aid that is tied to procurement from the donor country. The Foreign Assistance Act of 1961, Section 604(a) requires A.I.D. to tie its procurement to U.S. sources unless certain determinations are made. Presidential directives in the Kennedy and Nixon Administrations made provision for sourcing procurement from both the U.S. and less developed developing countries and, in certain circumstances, from other free world countries. The latter, however, require a waiver.

Mixed Credits. Mixed credits combine an unsubsidized export credit loan or guarantee with a grant from an aid agency. Mixing a grant and loan effectively subsidizes export credits whose rates are regulated through an Organization for Economic Cooperation and Development (OECD) consensus agreement designed to level the playing field. Since the early 1980s the U.S. government has attempted to reach agreement among all donors to end the practice of mixed credits. This effort continues under the Bush Administration. At the same time we must note that:

> Our competitors have increased their use of mixed credits almost four fold since the early 1980s while U.S. spending for capital projects declined.
>
> A recent Center for Strategic and International Studies study estimated that U.S. exporters lost $2.5-5 billion of business annually due to mixed credits offers that the U.S. was unable to match. An Administration study chaired by Eximbank, and released in April 1989 calculated the loss to U.S. exports in the $400-800 million range. This study also included a different method of analysis which found the loss to U.S. exporters from mixed credits to be diminimus and U.S.

> market shares remained stable in key markets.
>
> The whole of the Japanese Overseas Economic Cooperation Fund (OECF) program is the equivalent of a "mixed credit" program as its terms are less than 50% grant and remains tied to Japanese exports. The fact that Japanese aid is less than 50% grant also means that their money is far less valuable than U.S. aid which is almost completely grant. This is important in considering the relative size of Japan's aid effort. If it were calculated in terms of real value Japan's aid would be shown to be about half the size of the current U.S. aid program.

Let me just emphasize two further points.

First, tied aid and mixed credits are not the same. Mixed credits are a specific type of tied aid. And tied aid is, in principle, the norm for U.S. assistance in the more advanced LDCs, but it is provided on a grant basis.

Second, A.I.D. and Eximbank are looking at new ways to collaborate, using War Chest monies to achieve good development. This effort is based on an agreement that A.I.D. will be involved only in projects that make development sense. Any mixed credit involving A.I.D. (a) must have a satisfactory economic rate of return to the host country, (b) U.S. technology must be competitive in the absence of mixed credit, (c) no particular U.S. firm may obtain special financial advantage (and the firm must make a reasonable contribution to the project) and (d) U.S. taxpayer must receive a good return on their funding through new jobs or overall U.S. growth.

A.I.D. recently decided to participate with Eximbank in jointly financing a telecommunications project being competitively bid in Indonesia. A.I.D. provided $12 million of Economic Support Funds together with $12 million of the Eximbank's War Chest to meet the minimum grant element required. This project involves AT&T technology, training and direct investment. It is sound development (Indonesia has fewer telephones per capita than any country in Asia, including China). It has a high payoff to Indonesia, higher than other uses of A.I.D. funds. And it generates $18 of U.S. exports for every one dollar of U.S. taxpayers money. The Indonesian Government, however, has recently decided to retender the project and we will continue to follow AT&T's prospects closely.

We feel that developing basic infrastructure including public sector services in telecommunications, power and transportation systems will be essential to sustainable growth throughout the developing world. In fact, A.I.D.'s experience suggests that there is seldom any diminution of development impact as a result of promoting U.S. economic interests in programming our assistance for advanced LDCs.

Conclusion

To the extent that U.S. assistance promotes economic growth in LDCs, it also promotes U.S. economic interests. Growing LDCs tend to become better markets for U.S. products. Economic growth, a laudible end in itself, does not always lead to commercial advantage at least in the short term. But the absence of economic growth certainly stifles all commercial opportunities for U.S. exports. A.I.D.'s emphasis on policy reform and sustainable growth is a necessary if not sufficient precondition of U.S. commercial advantage. More directly, a significant portion of the goods, services and technology transferred to LDCs through any A.I.D. program are obtained from U.S. sources.

Many go further and think that economic self interest should loom larger in the foreign aid program. Economic growth is important especially in the poorest countries and they too could eventually become important partners as they grow.

Many advocate that more should be done to improve U.S. international competitiveness. The competitive threat of the Japanese assistance program is often pointed to, both because of

At the same time we must all recognize that A.I.D.'s primary mission is not export promotion. We have been and will remain a development institution. We will also continue to be involved in a wide range of countries each of whose requirements will vary. In many of these countries "mutual benefit" programs that involve direct benefits for U.S. businesses will probably remain small. The point being that we have many different objectives and economic self interest will not loom large everywhere.

But in many developing countries, particularly the more advanced ones, greater emphasis on economic self interest is likely to produce a better development impact. Early aid successes in West Europe and the Far East were predicated on such an approach. We have long recognized assistance should be seen as a transitory bridge to sustainable trade and private investment flows. The fact that our bilateral assistance program has become marginal in terms of the overall flow of public and private resources to many countries is an indication of success not parsimony on the part of the U.S. taxpayer.

Because our resources are limited and must meet competing objectives, A.I.D. will have to leverage any resources devoted to mutual benefit objectives. Wherever possible we will have to rely on capital project funding available from the multilateral banks and, even more important, U.S. business and the private capital market. I personally do not feel that it is enough to spend a dollar to generate a dollar of exports. We also have to avoid displacing commercial relationships with aid relationships.

The bottom line is that we can do more in many countries. To be effective, A.I.D. will have to collaborate with others in the U.S. Government and outside it. We will also have to remain committed to sound development projects and strategies: an approach which I believe also makes good business sense. And we will also have to recognize the competitive realities of the 1990s, realities that include tremendous opportunities in many parts of the developing world as well as competitors who have done better at linking their development assistance to economic self interest.

Mr. **Obey**. Thank you.

JUSTIFICATION FOR TRADE AND EXPORT AGENCIES

Let me ask a couple of boilerplate questions before I get to specifics. First of all, if some member on the floor or one of our constituents says, "Good God, why are we putting this money in these agencies? It is a capitalistic system; people ought to be able to stand on their own two feet. Why are we putting money in these programs when there are so many other competing needs?"

I would ask all of you to respond very briefly to that. Why should we have an Export-Import Bank at all? Why should we have OPIC? Why should we have TDP? Why should we do any of it?

Mr. **Lawson**. Well, let me have a crack at this first, Mr. Chairman, and I will keep it brief so others may chime in where I fear to tread.

I would start off by noting that in a perfect world we would not have an Eximbank. In a perfect world we would not have armies, we would not have IRS, we would not have a lot of things. But it is not a perfect world, and the fact of the matter is that out there in the marketplace foreign government subsidies do support foreign exporters, and you have to fight fire with fire.

Otherwise, it is not a level playing field. Bids are not going to be decided, on the basis of price, quality, delivery, after-sale services, et cetera. It is going to be decided on the role of foreign governments, and that is not fair. And that is basically the reason why we have Eximbank.

Mrs. **Rabb-Ayres**. Mr. Chairman, speaking for TDP, this is an easy question to answer. We do offer assistance for developmental projects, but the assistance does come through U.S. companies, and we are encouraging the development of our domestic economies as well through the use of TDP funds.

I am looking at a printout of one single project in Thailand and there are over ten States that have companies that benefit, that actually participated in the implementation of that project.

Mr. **Berg**. Mr. Chairman, I think one element of your question was why should we spend money to support these agencies? In that sense, with regard to OPIC I would say that what we are about is finding out, from Congress ultimately, just how much of our existing reserves we can dedicate to the idea and to the programs of investment promotion.

Mr. **Obey**. Well, why should you exist at all?

Mr. **Berg**. I think we should exist at all because when Americans invest abroad they do so for very good capitalistic reasons, as you pointed out. With OPIC support they can have their risk mitigated when they operate in the developing world.

And the United States can also see that our foreign policy objectives are advanced by actions of the American private sector abroad, particularly as it relates to developing countries creating exports and earning hard currency. We make sure that our projects have those developmental effects when we support them. That is our primary reason for existence.

Mr. OBEY. Again, primarily for the record, I wonder if each of you would simply lay out how your program works. In the case of Exim, how do you get plugged in? What is the process? Explain how a businessman would get you into the act?

Mr. LAWSON. For the record? Did you want me to do that for the record?

Mr. OBEY. No, go ahead for now. You can expand for the record if you want.

Mr. LAWSON. Well, I would be happy to expand for the record here. But briefly, an exporter simply calls up the Bank and says: I have a U.S. export. And we ask three or four questions here: Is it more than 50 percent U.S. content? Is there evidence of foreign subsidized competition? Is the transaction commercially viable? Is there a reasonable assurance of repayment? And lastly, would there be any adverse impact on the U.S. economy?

If those questions can be answered yes, then we will proceed right ahead with the request. It can be, I might add, not just a U.S. exporter; it can be anybody that wants to buy U.S. exports. It could be a foreign buyer, it could be a foreign private company, it could be a foreign bank to pass it through.

It could be most anybody who wants to buy a U.S. export. The system is really quite simple.

I might add that since John Macomber and I arrived at the Bank six or seven months ago, we let loose a task force to try to streamline the decisionmaking process of the Bank. Both of us felt that the case processing time was taking way too long, and there was a lot of paperwork. Cases were brought before the Board that should hve been handled at the loan officer level. You either trust the vice president and the loan officer or you do not, and we do.

So we set loose this task force. They came up with a report two weeks ago, and I am pleased to say that we are going to implement that. And I do not want to try to overpromise, Mr. Chairman. You always get in trouble when you overpromise. But, I think that within three to six months the case-processing time at Eximbank will be reduced by 50 percent, and that will be of great assistance to the U.S. exporter.

Mr. OBEY. How about TDP?

Mrs. RABB-AYRES. Mr. Chairman, there are a number of ways that one can access TDP. On the project level, we do hear about projects from the U.S. embassies abroad, directly from U.S. business, as well as from individuals.

Our first step in considering a project is to send out a definitional mission. This is most, if not all, of the time small companies that we contract directly with. We have a data bank of U.S. small companies, of consultants and engineers, and we put the definitional missions out for competitive bid, and any U.S. company that wishes to be on our data bank, we are pleased to have them. So we do have direct contracting as well.

Once a project is—once we have signed a grant with the foreign ministry for a feasibility study, we then advertise that study in the Commerce Business Daily. U.S. companies interested in responding then put together their bids and they send their bids in to the host government, but the advertisement is in the Commerce Business Daily.

As far as implementation of the projects, we are working on a number of ways of getting that kind of information out. Certainly we can be accessed directly by telephone. We are also working through state development authorities, working through the Department of Commerce and developing other means of information dissemination.

Mr. OBEY. And how about OPIC?

Mr. BERG. I think, Mr. Chairman, probably our most effective way of outreach is through our investment missions program, like the investment mission to Panama that I described earlier. We do five or six planned investment missions a year, and in the last several months we have done some additional investment missions of a rapid response sort in order to respond to new opportunities in places like Eastern Europe and now in Panama.

We have an Opportunity Bank, we call it the O-Bank, which is a computerized data base that matches American companies, who have expressed an interest in investing overseas as part of their growth strategy, with investment opportunities that we find out about from any of a number of sources, including, but not limited to, the United States embassies that are maintained in some 150 countries abroad.

I think with that data matching, with our outreach through investment missions, and with our outreach into the United States investment communities, and cooperation with State and local governments, we try very hard to make information available about what programs are and what we can do.

EXIMBANK FUNDING FOR EASTERN EUROPE

Mr. OBEY. Let me ask a question with respect to the funding that we provided last year for Eastern Europe. We had a $40 million OPIC package for Poland and Hungary. We had a TDP program of $2 million and an Exim trade insurance program. Would you give us a status report on the use of that money? What have you been able to put to use so far? What are your expectations about using it all by the end of the year?

Mr. LAWSON. Under SEED I here, one of the things that the Congress mandated was to establish a TCIP, a Trade Credit Insurance Program, for $200 million for short-term private sector. And I am pleased to say that next week AID and Eximbank will sign an agreement that will go into effect.

In addition to that, the Eximbank is adding on $200 million in short-term insurance for both the public and private sector, because in Poland, as the Chairman knows, it is a little bit tough sometimes to distinguish between public and private sector individuals as the focus of power and leadership is shifting back and forth and it is in a state of flux.

So we have added $200 million, onto the TCIP of $200 million.

Secondly, we are taking a very careful look at what Poland really needs, and what Poland really needs in my view and in the view of John Macomber and the team that went out to Poland in

December was medium-term credit. We are presently giving that a very, very careful look, Mr. Chairman.

I anticipate that——

Mr. OBEY. You say they need medium-term credit?

Mr. LAWSON. Yes, sir.

Mr. OBEY. You mean they need that this year?

Mr. LAWSON. They need it as soon as we can get it in place, yes.

Mr. OBEY. Well, given what happened in the conference last year, what shape are you in to provide that?

Mr. LAWSON. I think we are in reasonable shape. Most of it is going to be guarantee authority, Mr. Chairman. It is not going to be loans.

If we take a broad look at Eastern Europe and estimate what is the demand there, we would give a ballpark figure of somewhere between $300 million and $500 million.

Mr. OBEY. What I am trying to get at from each of you is this. As you know, the Senate subcommittee was talking yesterday about moving some of the Administration money requested for Panama and Nicaragua to Eastern Europe. I want us to do everything we can possibly do for Eastern Europe. What I want to know is your best professional judgment on this situation?

I am not asking for the Administration position. What I want to know is, if you had more money beyond that which you had already been provided by the Congress for this fiscal year, could each of you tell me flatly that you could not use it in this fiscal year?

Mr. LAWSON. Mr. Chairman, I do not think there is a single individual, a single agency head in the Bush Administration, that would come before you and say that they could not use more money, and Eximbank does fall into that category.

Mr. OBEY. I mean for Eastern Europe for this year.

Mr. LAWSON. For this year?

Mr. OBEY. If we provided additional running room, could you use it?

Mr. LAWSON. Yes, we could. The answer is an assured yes. I can give you a longer yes if you would like it.

We have taken a guesstimate of what would be the demand under SEED I and SEED II, which I take in process here, for all of Eastern Europe, and again I want to emphasize that this demand is a guesstimate.

Mr. OBEY. I am talking about use before October.

Mr. LAWSON. Yes, sir, I understand, I understand. And let me expand a little bit beyond October, if I may. But for the rest of the calendar year, our estimate would be a total demand for Eastern Europe of about $300 million to $500 million.

Now, that is total. That is loans, guarantees, and insurance. That is very rough and it is based somewhat on an estimate that U.S. market share would be about ten percent of, what is it, about a $4 billion market that the export credit agencies are already doing in Eastern Europe. And it does not include the Soviet Union.

Mr. OBEY. Would you have to turn anything down that you expect the Eastern Europeans to ask for between now and October 1, if we would not give you additional authority?

Mr. LAWSON. Yes. We are a demand-driven, first come, first serve bank, as you know, and that is the way we operate. We have scarce resources and we have got to be very careful about how we husband and use those resources. So the answer is it is quite possible that we are going to have to be extremely discriminating and selective, and some difficult choices are ahead of us, yes.

TDP AND OPIC FUNDING FOR EASTERN EUROPE

Mr. OBEY. How about TDP?

Mrs. RABB-AYRES. Mr. Chairman, in Hungary and Poland we have two draft grant agreements outstanding. We are awaiting the go-ahead from both countries in the telecommunications area. In Hungary the grant is $525,000; in Poland, $700,000. That could happen any day.

We also have a strong potential for a $400,000 grant in Hungary in electrical distribution.

Frankly, we have been calibrating our efforts in Eastern Europe. We already are looking at, just in those three projects, $1.6 million. I expect that we will be spending more than $2 million this year. However, we are calibrating our efforts. We are trying to figure out the most effective way to utilize the funds that we have.

We certainly expect to use the funds that we have this year in Eastern Europe, and there is a great deal more that we could do.

Mr. OBEY. How about OPIC?

Mr. BERG. You mentioned the $40 million earmarked investment guarantee. We will use all of that this year and it will be distributed in two projects: an Eastern European Growth Fund, which ultimately will be paired with private American capital, we think at a level of between $175 million and $200 million overall, to finance OPIC-style projects in Poland. This will be an Eastern European Growth Fund, so it will have applicability in other countries also.

The second project is a small loan facility. Our smallest loans are still too large to serve an increasing segment of the American small business community, so we are thinking that under an investment guarantee we can generate even a greater number of very small loans for Poland. We will commit the $40 million to those two initiatives.

Beyond that, in 1990, under the assumptions that you mentioned, shifting from Central America, we still have to face a project-specific demand in Eastern Europe: Poland; Hungary, where projects are coming on-stream more quickly; and ultimately we think this year given the expected Congressional action on SEED–II, Czechoslovakia; and beyond that, depending on other circumstances, the other Eastern European countries.

So the demand is there, I think, for the investment.

MEDIUM-TERM CREDIT CEILING

Mr. OBEY. Is the medium-term credit ceiling a problem for any of you? I guess it would be for you.

Mr. BERG. No, it is not. I think it is at Eximbank.

Mr. LAWSON. Well, the medium-term limit of $215 million, is a problem because it does reduce our flexibility, yes, sir.

Mr. OBEY. It does reduce your flexibility in Eastern Europe?

Mr. LAWSON. Absolutely, yes, sir, Eastern Europe and right across the board, obviously, but certainly in Eastern Europe.

Mr. **Obey**. We had one hell of a fight with them on that.

Mr. **Lawson**. I know you did and I appreciate all the help that you gave us on that.

Mr. **Obey**. I have taken more than my time. Let me just ask one quick question on a topic I will eventually get back to later in the hearing.

When we asked the Eximbank for several years to reserve against their losses, Paul Volcker went around this town like the Great Oz saying that the walls would crumble and the ceiling would fall and the world would come to an end if that happened. Has it?

Mr. **Lawson**. No.

Mr. **Obey**. Has anybody told Mr. Volcker?

Mr. **Lawson**. I would be happy to call him and tell him if you want me to, Mr. Chairman.

Mr. **Obey**. I hope he has taken due note.

Mr. Gallo.

Mr. **Gallo**. Thank you, Mr. Chairman. I know of your interest in this and your commitment, which I also share with you.

FINANCING U.S. EXPORTS

I would like to take this opportunity to welcome Mr. Lawson and the rest of the panel. We have been having through these programs, Exim and TDP and OPIC and AID, all success stories, and I do not think that there is any question that they do strengthen our economic interests and at the same time help developing countries.

But I think far too long American companies have had the best products at the best prices, but have not been able to compete because of lack of financing or at least competitive financing. And it becomes more and more evident to me every day when I get calls in my office and both major and middle-sized companies say that, we have been successful in our product, we have been successful in the bid so far as price, and we have lost out as a result of financing.

And that annoys me and it, I am sure, annoys you. We have that problem coming up more and more frequently. With a $100 billion trade deficit, we cannot afford to be left out of the new markets throughout the world.

And the Export-Import Bank is one of the keys to our ability to compete, along with, as mentioned, the different segments that also help in bringing about American trade and exports. I know the Eximbank is doing the best it can with the limited resources, and I have a number of questions that I would like to ask dealing with, first, Japan.

When I look at our amount in the export-import area of $500 million this year—it was $615 million—it kind of pales when I take a look at Japan's, which is estimated at about $4.4 billion. And at the same time, we want other countries to be involved in these developing democracies and certainly we do not want to dissuade other countries to get involved.

But most of their involvement is tied to trade guarantees, something that we have not done.

I am wondering what your thoughts, Mr. Lawson, on that, how we can better compete with the limited amount of moneys we have to assure that our companies in the United States are going to be in that competitive position?

Mr. **Lawson**. Well, Mr. Gallo, that is a very thoughtful question. Let me see if I can give a reasonably thoughtful answer to it.

First of all, as people in this room well know, the savings rate in Japan is about three times what it is in the United States, and the cost of capital in Japan is so much cheaper, and that is of course what drives the interest rates here and makes our commercial banks unwilling to participate in trade finance.

Eximbank is a small bank with small resources, and we cannot possibly hope to support all the U.S. exports that are worthy of being supported. So we are going to have to devise ways to draw the money center banks in New York and the big regional banks back into trade export finance.

The way you do that, I think, is to drive those interest rates down, and that takes a little bit of time. And we are working on that, as you know.

Having said all that, we are faced here with a very severe budget restraint environment and, like every other government agency, we are just going to have to step up to the plate and take our lumps here. We are going to have to learn to do more with less.

There are several things that we are doing right now. One is called Bundling. We just announced that last week in connection with an Eximbank guarantee we are providing on U.S. exports to Mexico, Bundling is where you take smaller export credit transactions and package them all together and put an Eximbank guarantee on it and then sell them in a package in the capital markets. This puts new money back in the country.

It is a very novel approach. It was worked out by Harold Meyerman at the First Interstate Bank and John Macomber. I think it is the wave of the future especially in reform countries like Mexico. It has got applicability to other countries around the world, too, the Philippines, et cetera.

We also are taking a good hard look at our guarantee program. We have, as the Chairman pointed out, ample guarantee authority, $10.599 billion. In the past, we have not utilized all of it. We have utilized 40, 50 percent. We have a good guarantee, but I think, it can be made even better. The problem gets into the fact that if you start to make it even better, then the CBO starts to score it as a direct loan. So you have to walk a thin line.

But there are, I think, ways to do that, and we are certainly exploring those. So I assure you that we are trying to be better and smarter and more imaginative with the money that we have.

Mr. **Gallo**. Let me just say that your program—the City/State Program—is a very worthy one and one that will complement the overall development of exports. What do you feel we are up against, though, when we are dealing with the Eastern Europe and the major trading partners? What do you feel we are up against?

Mr. **Lawson**. I think the number one problem that the U.S. exporters face today is trade financing. As you put it well in your opening statement, U.S. industry these days can compete extremely well in almost every single industry. We do not have to compete in every single one, but we do a very good job in most major capital goods industries and lots of other industries, too, in terms of price, quality, delivery, after-sale services, et cetera.

Secondly, the dollar is probably in better balance today than it has been for a very long time.

Where we are not competitive is in trade financing. So we are working right now with the Japanese, in fact with the Japanese Eximbank, to help them, as it were, recycle their so-called surplus Nakasone yen, and we are making some progress in that direction. Maybe not quite as fast as we would like, but we are making some progress in that direction. They simply have the money to do it and we do not right now.

Mr. GALLO. Well, I know that they are committing about $500 million per year to these countries, which is a sizable amount. And with that $500 million, they do extract trade agreements or at least understandings, and I think that, especially when we have a limited amount of funds to help our particular industries, it is important that we utilize every technique that is available in developing that.

Mr. LAWSON. I agree.

FOREIGN ASSISTANCE AND U.S. EXPORTS

Mr. GALLO. A question to Mr. Brown. In your area of expertise, how much in U.S. exports is generated from each dollar spent by A.I.D.?

Mr. BROWN. That is a tough question. We have a number of estimates and are right now engaged in trying to come up with a more precise answer. Some of the foreign assistance programs like P.L. 480 for example, are derived entirely from U.S. sources. The American farmer reaps almost 100 percent of the benefit of that program. As regards to shipping, over half of the shipping of P.L. 480 commodities is on American ships.

In the Economic Support Fund account, that portion which is projectized is often used for capital projects finding. As I mentioned in my written testimony, much of the projectized ESF results in export business for American companies, a good example being Egypt. The actual numbers were mentioned in my written testimony.

The commodity import program in the ESF accounts also directly benefits American business.

Where we have some difficulty in coming up with an exact tally—and I have seen varying numbers on this—is on the procurement side. A considerable amount of discretion regarding procurement is left to our overseas missions. We have made some recent attempts to quantify it, specifically in a recent inquiry by the GAO. We went to six countries in an attempt to count procurement dollars and got varying results from each country. It was around 50 cents on the dollar for those six countries.

In Africa, the Development Fund for Africa is not required to procure from U.S. sources. Nevertheless our last count there revealed that roughly 50 percent of procurement of goods and something like 80 percent of services went to Americans firms.

There was another case study that was done in Thailand by a contractor, where the number was a lot lower on the procurement side—it was 20 percent or so.

We are now attempting to undertake more studies in more countries to come up with an exact procurement number, but I cannot give you an across the board number at this time.

Mr. GALLO. Well, what is your views towards that as far as linking the aid to increasing the U.S. exports?

Mr. BROWN. Well, as I indicated in my testimony, I see nothing wrong or incompatible with pursuing good development programs overseas using American technology, American business, and American exports. We have some of the best technology and some of the best products.

After all, what are we really doing with the aid money? We are transferring something from America to these countries in order to help them develop. There is nothing wrong with using American goods and services where compatible and where possible. After all, the law requires it.

Mr. GALLO. I think your statement was a very strong one in dealing with the private sector and I concur with you. I know that in the more advanced developing countries there is a great need for telecommunications projects and I know for a fact that many companies in the United States have that expertise.

And I would hope, if we are going to get directly involved in a major shot of money in aid in that area, that we certainly do not go below a 50 percent figure. To me, I have heard the 20 percent figure, which kind of outrages me.

Mr. BROWN. Well, as I indicated, that was a one-case study and I doubt it is representative. However, that situation is what moved us to look at other situations, and we have not found that low a number in any of the other countries that we have looked at.

ADMINISTRATION'S BUDGET REQUEST

Mr. GALLO. Mr. Chairman, if I could just close my questions out by saying, I know that each one of the panelists in their areas have an important role and play an important role in developing better relations and also direct involvement by the private sector from the United States.

I for one am not happy with the amount that the Administration has put together. I think we have tremendous opportunities. When I look at that balance of trade deficit, then I look at what we are trying to do to bring about opportunities for American companies, and what that means in new employment, not to say the revenue base that comes out, I think we are short-changing our companies and we are short-changing the United States.

But I thank you for your comments and your statements.

Mr. OBEY. Thank you.

Mr. McHugh.

Mr. MCHUGH. Thank you, Mr. Chairman.

Let me say first of all I think that your programs are very important ones. I think the subcommittee supports them and I associate myself with the remarks of both the chairman and Mr. Gallo, who have indicated that, expressly or implicitly, that the request here may be inadequate to deal with the kinds of playing field problems you have described. And the Export-Import Bank is a good example of that, but I think the other two agencies are also good examples of where we need to be perhaps doing more.

USING FOREIGN AID FOR PROMOTING U.S. EXPORTS

Frankly, Mr. Brown, I am very concerned about your philosophy on aid, if I understand it. Unlike these other three agencies, I do not think that development assistance or even ESF should be a primary tool for promoting American export contracts abroad. I do not think A.I.D. should be used for mixed credits.

Now, that is a distinction. I am not suggesting that when you do development work in poor countries that we should not have the byproduct of American goods and services being purchased. In that sense, I agree with Mr. Gallo. I would hope that when we are focusing on development in poor countries that there will be that byproduct, that American goods and services will be purchased with American aid funds. That is not the problem.

What concerns me is, as I understand mixed credit programs, that the basic purpose is to sell the American contract, to get the deal closed. The basic fundamental goal is not necessarily to spend that money on the best possible development project.

In other words, the fundamental goal of mixed credits is different in some cases than the fundamental goal of A.I.D.'s development assistance programs. And I do not want an A.I.D. program that is driven primarily by export contracts, because we will have private companies coming to us all the time, as well as to you, to get assistance for their contracts, for their export deals.

It is perfectly legitimate for them to do so. That is their business. But it is not the business of A.I.D.

And I can tell you in political terms, the people in this Congress who are the strongest supporters of your economic assistance programs are Democrats, and if Democrats get the notion that your program is no longer driven by dealing with the development problems of the poorest countries, that it is being driven by AT&T and other American companies who are trying to close their deals, you are not going to pass a foreign aid bill in this Congress.

So from your perspective in that sense, I think you better be very, very careful.

Now, I support the war chest for Eximbank because those other countries are out there subsidizing their trade. And we cannot be naive about it. We have to be aggressive. And I will support as much money as it takes to compete or even the playing field in the export trade market. So I am not against voting money for that purpose.

But I do not want the aid program, which has another purpose, traditionally has had another purpose, eaten up by this trade purpose. I want to keep a firewall between those two legitimate concerns.

But from what I see in your statement, you are suggesting that A.I.D. has a pot here which has not traditionally been used for trade export promotion, but which should be. And I want to tell you, I firmly disagree with that position if I understand you correctly.

For example, one of the things that raises my concern is in your statement on page 2 you are indicating by way of example what the Japanese do as compared with what we do, and you say in the first full paragraph on page 2: "Another way to consider the link between current A.I.D. programs and U.S. exports is to consider the country allocation priorities. The top five developing country importers of U.S. capital goods in 1988 received less than one percent of total economic assistance versus 24 percent of total aid in 1962."

Well, I think that is good. It suggests to me that the people, the countries that we were providing foreign assistance to in 1962, have now graduated by virtue of economic growth, hopefully in part because of our aid, to the point where they are now buying from us. Their economic growth has been such that they are now customers of the United States. Well, that is fine.

I do not think we should be pumping more economic aid into those countries when you have countries in sub-Saharan Africa that are still desperately poor and underdeveloped. Do you see my point?

Mr. BROWN. Yes.

Mr. MCHUGH. You are correct, Japan does this. Your next sentence says for Japan:

> Their top five developing country markets [Korea, China, Thailand, Malaysia, Indonesia] received 30 percent of their aid in 1988.

Mr. BROWN. That is the point I am trying to make.

Mr. MCHUGH. Yes. Well, the Japanese do do it differently than we do, and I think we should fight the Japanese in that respect. But we should do it with the Eximbank and with these other agencies that are trade promotion agencies, and I support them.

But I do not want you to become primarily a trade promotion agency. I want you to be a development agency and focus on those most underdeveloped countries, as in sub-Saharan Africa, that are not getting adequate resources today, in part because we have limited resources. And I want those limited resources focused on where the underdevelopment problems are the most serious, and not have those limited resources eaten up by trade promotion goals, which are perfectly legitimate goals, but which should be undertaken by these other agencies.

So your presence and your statement gave me the opportunity to make the point. I am not sure everybody agrees with me on this, so I may be speaking only for myself.

But I can tell you that I have been a strong supporter of economic development assistance. I think it is an important tool of American foreign policy, one because it is humanitarian, and two, because it ultimately promotes, as your statement says, the kind of economic growth that is in our national, as well as the recipient's, interest.

But I will tell you something: I will be an opponent of this program if I find that it is being eaten up for trade promotion purposes by these other agencies which are in that business and which deserve our support for their goal. I do not want to see A.I.D. become another trade agency.

Well, I think I have probably eaten up all of my time in giving you that sermon. But I would be happy to give you the chance to respond in any way you would like to, having listened to me now for five or seven minutes.

Mr. **Brown**. I do not intend to make a speech, but to point out that the record seems to indicate the opposite. We have certainly not become a trade promotion agency. We are not a trade promotion agency, and there is nothing I have said to indicate that we are.

Mr. **McHugh**. No, but your philosophy expressed in your statement suggested to me that you would like to go in that direction.

A.I.D. AND MIXED CREDITS

Mr. **Brown**. The reference I made is that we are working very closely with the Eximbank in programming the war chest. Our policy is to take a very proactive stance with the OECD, to try to get them to change their practices. And unless we do that, it is very unlikely that there is going to be much movement on their part in changing their practices.

We have worked closely with Exim in finding activities that have good development potential that the war chest might fund.

Mr. **McHugh**. That is great. I have no problem.

Mr. **Brown**. We also have the authority to do some mixed credits. There is a limit of $5 million per year. $5 million per year out of a total budget of close to $6 billion is not a major portion of our program.

Mr. **McHugh**. That is right and I have no problem with that, either, except to the extent that it is the camel's nose under the tent.

Let me ask you two quick questions here. Number one is, you are not claiming that there is existing authority, are you, for more than $5 million?

Mr. **Brown**. No, I am not claiming that at all.

Mr. **McHugh**. Of either development assistance or ESF money? I do not think there is, either.

Secondly, would you like to see A.I.D. be able under the law to use more than $5 million for mixed credits?

Mr. **Brown**. I think that we could effectively use more than $5 million for mixed credits, while at the same time promoting good economic development in virtually every country in which we have a development program.

Mr. **McHugh**. Why not increase the war chest for the Eximbank and have the Eximbank continue to work and consult with you as to how that might best be used?

Mr. **Brown**. I have no disagreement in principle with doing that. We can provide Exim with our expertise on development. It is key that these mixed credit activities have developmental benefit.

The AT&T initiative in Indonesia is one example.

Mr. **McHugh**. You understand I have no quarrel with that. That is fine. My concern is that the more we earmark in your programs for trade promotion, mixed credits, the more it takes away from your traditional development money and focus. So I am all for giving the Eximbank what it needs and having them work with you because that is their goal and I support it.

But I do not want to see more money in your programs, which are limited already, being used for trade promotion. I want to distinguish that from when you engage in basic development work, having the benefits of goods and services being purchased here in the United States come back to us. That is fine. Like Mr. Gallo, I think that should happen.

But that is different than saying our decision about how this program money is going to be spent is going to be made primarily on closing the contract, as opposed to primarily made on what is the most important development work that we can do in X country or X region.

My time has expired and thank you for listening, and I hope that we can come to an understanding on this.

Thank you, Mr. Chairman.

Mr. **Obey**. Mr. Porter.

TELECOMMUNICATIONS IN EASTERN EUROPE AND INDONESIA

Mr. **Porter**. Thank you, Mr. Chairman.

I am sorry I missed this good debate that has been going on here. Maybe this question will define it a little bit further. Mr. Brown, last year we targeted about $25 million of money for Eastern Europe to go to telecommunications projects, and this money as I understand it is to support only private sector projects.

But all of the telecommunications infrastructure in Eastern Europe is owned by the state. So how would a U.S. company be able to win, say, a Polish PTT project using this money?

Mr. **Brown**. Using the $25 million? I gather you are expressing a slightly different view than that by Mr. McHugh before.

I will have to get back to you with that for the record.

Mr. **Porter**. It seems to me it is a serious problem that I really would like you to look into and give us an answer.

Mr. **Brown**. I will furnish that.

[The information follows:]

The SEED Act authorizes the Polish-American Enterprise Fund to use up to $25 million for grants for projects providing for the early introduction in Poland of modern telephone systems and telecommunications technology, which are crucial in establishing the conditions for successful transition to political democracy and economic pluralism.

The Enterprise Fund is a private organization whose purpose is to promote development of the Polish private sector. The organization has broad discretion to decide what and how it will promote the private sector. There is no statutory prohibition against its becoming associated with activities that involve State owned segments of the economy, when doing so will be an effective way to promote the private sector.

I am confident that the Fund's directors will give serious consideration to the SEED Act provision on telecommunications and will do what it finds appropriate and sound in the light of its analysis of the situation and its statutory mandate.

Mr. **Porter**. Mr. Lawson, it is my understanding that our war chest is being used in a huge competition for telecommunications equipment in Indonesia on behalf of AT&T, and can you give me an update on how we are going to win that contract?

Mr. **Lawson**. I would be happy to insofar as I know the details of it. As you know, it has been re-tendered. I was in contact with the

U.S. embassy in Jakarta and Mr. Macomber was just there three weeks ago at the same time that this deal was before the President of Indonesia. We do not, however, know the reasons why it was retendered.

We are hopeful that in the re-tendering that AT&T will continue to be competitive. As you know, the U.S. government was highly supportive of it. We turned ourselves into a pretzel here to make sure that the mixed credit tied aid met the provisions, and AT&T was awarded the contract or was recommended to the President on the basis of price, quality, delivery, et cetera.

So we just keep our fingers crossed, stand on one leg and hope that they will emerge successful.

Mr. **Porter**. Thank you.

ENVIRONMENTAL CONSIDERATIONS IN TRADE FINANCING

Mrs. Rabb-Ayres and Mr. Berg, can you tell me how you factor the environmental concerns into your decisions regarding the type of aid that you provide, the type of development and trade aid that you provide?

Mrs. **Rabb-Ayres**. Mr. Porter, we do a great deal in the environmental area, directly and indirectly. That is always a consideration in our assessments. We are doing a great deal on clean coal technology, air and water, environmental concerns. A number of the projects we consider are backed by World Bank funding and the World Bank requires that the project be highly responsible in terms of the environmental impact.

So we find that, in addition to projects that deal directly with environmental concerns, all of the industrial projects that we work on are environmentally responsible.

Mr. **Berg**. I would say, Mr. Porter, that with regard to the OPIC projects that we finance or insure, all of these projects go through a multi-screen process within OPIC before we commit to them on either finance or insurance, and one of those screens is a very elaborate environmental analysis.

We actually look at what the downstream effects will be on the environment in the country in question, and we also consider what the project might have to comply with if it were taking place here in the United States, in order to provide some sort of context for the environmental analysis that we provide.

I might also say that we are trying to give support and opportunity and information to American companies who are in the environmental field. It is a very interesting, horizontally integrated field that is emerging in this country, all the way from waste management to waste disposal, to clean industry technologies.

We are going to create a venture capital fund, pairing our contributions with U.S. private capital to finance projects in the environmental area around the world. We think this will provide a new opportunity for American companies to participate in these projects in countries that do not have anywhere near the level of formal protection in the environmental arena that we have, but that have much more serious environmental problems.

Now, I am not saying that we should encourage our companies to operate in a less than environmentally sound area. But American technology has been designed to operate in this country, and I think if we can bring that technology to the environmental problems abroad in developing countries we are doing several things: We are providing an opportunity for U.S. companies not only to invest, but to export their technology; and (2) we are also bringing into these new and developing markets our own sense of what you need to do to protect and preserve the environment.

Mr. PORTER. That is good news.

RESPONDING TO GLOBAL CHANGES

Finally, for those of you who want to answer it, we have seen a lot of changes, very sudden changes, in the world over the last year and a half or two years. There may be a possibility that Cuba may be moving over to an open system some time soon.

Do you have any contingency plans of what you are going to do in the event that that occurs? Anybody been thinking about that?

Mr. BERG. I will wade in. We have. We are ready to send an investment mission to Cuba as early as next week.

No, I think in fact, as I mentioned earlier, we are looking at resources in order to try to position ourselves to promote American investment into a place like Nicaragua, which took an unexpected and for this country very beneficial turn in its elections.

The situation in Nicaragua has heightened our awareness of the fact that Cuba will change. I do not think there is any question about it. Cuba was once a tremendous market for American investment and certainly for American export, and I think it will be again. And, I think that American export and American investment into Cuba will be the thing that will turn that economy around from its absolutely devastated state right now.

So for OPIC in terms of looking at the possibility for American investment, I think we would be ready to start to mobilize our programs for Cuba when we can.

Mrs. RABB-AYRES. Again, that is an easy question for TDP. Of course we are all aware that Cuba may open up, and there are a number of other countries, and that is the kind of an opportunity that we are prepared to respond to immediately, as we did in Panama and Eastern Europe.

If I might just take this opportunity to respond to an earlier question that you directed to Mr. Brown in terms of telecommunications, I can give you just an initial answer. TDP is very active in telecommunications in Eastern Europe. There is definitely a very strong desire for U.S. participation, and in both countries that we are active in, in Hungary and Poland, there is existing in some cases and pending legislation to allow for private participation in the development of the telecommunications systems.

So there will be opportunities in terms of private participation. And I have also been assured by officials in Poland that in fact there is an active private sector in the telecommunications area. Albeit small companies, they are there.

So I am confident that in fact this money can be well spent.

Mr. PORTER. Well, I appreciate that. I am particularly interested in the $25 million that A.I.D. has, however. We do need an answer on that.

Thank you very much.

ROLE OF EXIMBANK IN SOVIET UNION

Mr. OBEY. Let me ask a question with respect to Exim at the risk of panicking the White House even more than they were panicked when Mr. Gephardt gave his speech two weeks ago. Has there been any thought given to conducting studies indicating the kind of Exim involvement that might eventually be fruitful within the Soviet Union. This is assuming that they were to achieve sufficient economic reforms, including currency convertibility and all the rest?

Has there been any thinking going on, at least any examination, of the potential there for U.S. business and Exim participation?

Mr. LAWSON. Yes, Mr. Chairman, there has been a considerable amount of thinking going on, because it is our estimate here that by the time of the June summit between President Bush and General Secretary Gorbachev that the Jackson-Vanik amendments may in fact be waived. Then you have the Stevenson and Byrd amendments which also have to be looked at.

Then a finding has to be determined by the President that it is in the national interest for Eximbank to do business in the Soviet Union. After that series of obstacles has been overcome, then Eximbank's Board must look at the Soviet Union as a credit risk and make certain determinations about its ability to repay whatever loan guarantees and insurance that Eximbank may wish to do.

Mr. OBEY. Well, what is your estimate of what kind of opportunity might lie there in the next ten years?

Mr. LAWSON. Well, I think there are lots of opportunities for U.S. exports to the Soviet Union. We have been talking to a lot of businessmen. The phone has been ringing with a lot of interest in doing business in the Soviet Union. Certainly in the oil and gas industry there, they are in desperate need of secondary and tertiary recovery in their oil fields.

There is a tremendous amount of U.S. exports that I think we could do business with there in the Soviet Union.

MEDIUM-TERM CREDIT CEILING

Mr. OBEY. We talked about the medium-term limitation. Would you lay out for us some of the specific problems presented to you by that limitation that were worked out last year?

Mr. LAWSON. Well, I think the bulk of our loans are in medium-term, and we can go to—we will be up at that $215 million cap probably the first month of the fourth quarter, and after that it is going to be a little bit tricky.

So I would very much be in favor, speaking for the Bank to have that ceiling really done away with. It does not allow us the flexibility to move into Eastern Europe or into Panama or Nicaragua or whatever place in the world we are looking at. In this fast-changing world that cap limits our ability to provide medium-term financing in these emerging democracies.

Mr. OBEY. If you were to describe and to quantify in a sentence or two to the Senate the negative impact of that, what would you say?

Mr. **Lawson**. I would say it is a handicap to the ability of the Bank to provide medium-term financing in a rapidly moving world.

Mr. **Obey**. I understand that, but how would you measure the damage?

Mr. **Lawson**. We are going to be losing some export business because of that.

Mr. **Obey**. But can you quantify that?

Mr. **Lawson**. It is very hard to quantify because, Mr. Chairman, we have at the Bank, as you know, cases that sometimes have a very long fuse. It is hard to know what cases are going to be done this year as opposed to next year. We have to make a determination on each case as to which year it is going to fall into.

Mr. **Obey**. For us to be credible in arguing their position, we have to be able to quantify it at least roughly. Otherwise, it is a theoretical discussion with no demonstrable impact.

Mr. **Lawson**. Let me see if I can help you, Mr. Chairman, on that. As I mentioned, we will be up against the medium-term cap the first week of the fourth quarter. That is our estimate.

Mr. **Obey**. And?

Mr. **Lawson**. And therefore after that——

Mr. **Obey**. What is the message which I can deliver to Mr. Leahy in the conference? In other words, why is what you are saying bad business, and what does it mean we have lost?

Mr. **Lawson**. It means that we will be losing—we will not be able to support medium-term credits for U.S. exporters after that, and we will definitely be losing some business. There is no question about that.

Mr. **Obey**. If you could expand on that more for the record, I would appreciate it.

Mr. **Lawson**. Yes, sir, I would be happy to.

[The information follows:]

If the ceiling on medium-term loans remains in effect, it is projected that the Bank would exhaust its medium-term loan authority by the fourth quarter of FY 1990, based upon the present rate of utilization. The medium-term loan program, which is very important in serving the needs of small and medium-size exporters, shows a fairly steady flow of activity, and is needed in order for U.S. firms to compete in a number of important markets.

The ceiling has not impeded our efforts to serve small business so far, but certainly would if we ran out of authority for a period of several months. If this happened, it would have a serious adverse effect on the ability of exporters of all sizes to compete—any time the Bank is put in the position of starting and stopping of offering loan support, it calls into question in the eyes of our customers, the foreign buyers, the capacity of the Bank as a source of required financing. Threats such as this question the dependability of the Bank and have severe long-term consequences that are very difficult to dispel.

INTEREST EQUALIZATION PROGRAM

Mr. **Obey**. Last year, as you know, this committee supported and the Banking Committee passed an authorization which provided for the initiation of an IEP program, an interest subsidy program. Our understanding is the Administration has decided not to start that program, even though it could have been used to finance upwards of $200 million this year and over $350 million next year.

How did that happen? Why did that happen?

Mr. **Lawson**. The Bush Administration at a meeting of the EPC decided not to proceed forward with the IEP——

Mr. **Obey**. For the record, would you explain what the EPC is?

Mr. **Lawson**. It is the Economic Policy Council, which is chaired by the President and in his absence chaired by Secretary of the Treasury Brady. This is a Cabinet-level body designed to iron out inter-agency disagreements.

The IEP was presented before the EPC and it was determined and decided by the EPC not to move forward with IEP this year. I think the reasons for that, Mr. Chairman, are severalfold. First of all, several people felt that it was a new program and that we did not want to start a new program in this budgetary environment.

Secondly, some people felt that the IEP is somewhat more expensive, which it is actually, than supplying direct credits, because the Eximbank of course borrows from the Treasury at a better price than the commercial banks, which have to borrow at commercial rates. So that is true.

I think some people viewed the IEP as a budget gimmick. Under the IEP, the subsidy is scored as opposed to the whole amount on a direct credit. It was felt that this was a budget gimmick in that regard, and that it really was not true credit reform.

So for all those reasons and two or three more, it was decided not to move forward.

EXIMBANK WAR CHEST

Mr. **Obey**. How much have you used of the War Chest so far this year?

Mr. **Lawson**. We have been using the War Chest, Mr. Chairman, very aggressively. We have already laid out in offers over $90 million of the $110 million that we have authorized.

Mr. **Obey**. I have another question for you for the record at this point on that.

[The information follows:]

Question. We were told last year that the Administration intended to use the *Mixed Credits War Chest* more aggresively than they have in the past. Now we see a request for a small increase from $110 to $114 million for the War Chest for 1991.

Would you tell us what negotiations have aimed at cutting other countries mixed credit practices this year and what results have come from those negotiations? Are we not being taken seriously because our subsidy program is too small?

Eximbank Response. Over the past year the Administration has mounted a significant action program to deal with the extensive use of tied aid credits by other governments for commercial advantage:

In April 1989, the Administration submitted a comprehensive report to the Congress concerning the practices of other governments and effects on the U.S. economy.

In September 1989, the Administration submitted recommendations to the Congress about its strategy for a new aggressive negotiating initiative in OECD to restrain tied aid credit use for commercial gain, combined with the initiation of U.S. tied aid credits in countries and sectors where U.S. exporters have been particularly damaged by the practices of other governments. Further, Eximbank "War Chest" grants and other Eximbank resources would be combined, where possible, with additional budget resources from the Agency for International Development and the Trade and Development Program to provide maximum benefit to U.S. exporters. It would also significantly advance the negotiating process. Any projects involving A.I.D. would also have a strong developmental purpose.

In December 1989, the Administration announced more specific guidelines for more aggressive use of tied aid credits to support its OECD negotiating strategy. The target sectors would be power generation, telecommunications, transportation and construction equipment, and the target markets would be in Asia and North Africa where tied aid is used extensively by other countries.

As part of the overall strategy, Eximbank continues to be alert to situations where other governments violate existing OECD rules, so that the U.S. can react with matching or over-matching tied aid of its own to exert discipline on others in following OECD rules.

OECD negotiations were begun in January 1990 and have continued in April. They are likely to continue through the next Economic Summit in June of this year and beyond. Meanwhile, the strategy to *initiate* U.S. offers in countries and sectors where the U.S. has been most damaged is viewed—by both the other governments with whom we are negotiating, and by U.S. suppliers—as a real change from our reactive policy of the last two years of responding only to violations. We hope for significant results from this two-pronged strategy of negotiating with new aggressiveness while we simultaneously act to protect our own trade interests.

EXIMBANK CITY/STATE PROGRAM

Mr. **Obey**. Would you tell us a little bit more about your state-level programs? What States have been active, and when are you going to be in Wisconsin?

Mr. **Lawson**. When am I going to be in Wisconsin? As soon as Wisconsin wants us, Mr. Chairman, we are going to be there with a vengeance.

I think that it is really one of the great success stories here at the Bank, and we are putting a great deal of stress on this City/State Program. We now have twelve different sites, twelve different States, actually eleven States and then the Port of New Jersey and New York. And we have substantial interest from at least six other States, if not seven or eight, Oklahoma being one of them, which is my home State.

I think this is the best way I know how to try to leverage our scarce resources. We do not have field offices here and we cannot cover everything.

Mr. **Obey**. You say you're from Oklahoma?

Mr. **Lawson**. Yes, sir.

Mr. **Obey**. Where were you born?

Mr. **Lawson**. Tulsa.

Mr. **Obey**. I was born in Okmulgee.

Mr. **Lawson**. Is that right.

Mr. **Obey**. Go ahead.

Mr. **Lawson**. We have looked long and hard at the best way to get out there to look at the 400,000 potential small business and medium-sized business exporters who want to export. And it is very hard for a Bank of our size, located here in Washington, D.C., to try to get out there and get the word around. Our marketing division is doing an awfully good job.

But the best way that we have come up with is to work with the governor's office and set up this City/State Pilot Program, whereby we ask the city-state to sign on with us to send two of their people back to Eximbank for a training period of three weeks, to put up a certain amount of money, and to get the governor involved, and to sign an agreement with us that they will stay the course for at least two years.

We have had a lot of success with that. I was just out in Washington State where I met with the Governor and we signed a city-state agreement, and the Governor is four-square behind it.

After all, those are resources at the State level that are going to be there for a while. While the Federal government's budget is somewhat constrained, the States' budgets vary wildly. So we feel that this is the best way to get out across this huge country to get at these people.

Barring that, we would be open for any kind of suggestions from you or anybody else as to how we can better leverage our resources to get at this. But I see in the future, Mr. Chairman, that the growth in U.S. exports is going to be coming from that sector of our economy. It is going to be coming from the small businessman, the medium-sized businessman.

And when I have traveled around this country in the last six or seven months, I see that there is waiting room only at these export seminars. A few years ago when I used to work at the Commerce Department, there was not. There was not that level of interest. But there is now.

So the word is finally getting out that it is important for the U.S. economy, important for our way of life, to increase our exports, and we are seeing this in the turnout for all these seminars and conferences.

TRADE AND EXPORT PROGRAMS IN CHINA

Mr. **Obey**. What about China? What are all of you doing in China?

Mr. **Lawson**. Should I go first?

Mr. **Brown**. A.I.D. is not doing anything.

Mr. **Lawson**. We now have about $420 million in exposure. The demand for China from our exporters has fallen off dramatically since June the 4th. It is not "business as usual" at the Bank. The Bank will process cases that come in only where the bid is imminent or where a U.S. exporter might lose the business if we do not process the case.

We now pass all those cases over to the State Department for alleged violations of human rights. So it is not "business as usual", but we are open in all of our programs there. The demand has simply fallen off tremendously.

Mrs. **Rabb-Ayres**. Mr. Chairman, TDP has not initiated any new projects in China since the events in Tiananmen Square. We are continuing, of course, with those projects where the contracts were in place prior to those events.

Mr. **Berg**. Similarly, we have stopped doing new business in the PRC since the events of last June. Prior to that, we had outstanding investment insurance of about $125 million spread over 32 projects in the PRC. We will, of course, continue to service those outstanding contracts.

We are also affected by the recent China sanctions bill, so OPIC would not recommence its programs in the PRC until those sanctions are changed, or the President, under the terms of that legislation, makes a finding that it is in the national economic interest of the United States for OPIC to recommence its programs.

MIXED CREDITS IN INDONESIA

Mr. **Obey**. I want to get back to mixed credits. I share Mr. McHugh's view that we do not want to see A.I.D.'s programs slowly squeezed into a situation in which we are taking our eye off the long-term need to establish development that works, rather than development that is temporarily convenient to us because it suits an American corporation. That does not contribute to getting somebody off the dole long-term. I think you can respect Mr. McHugh's concerns and still deal with the real world of competition if you simply increase resources that are used through ESF solely for that purpose. My concern is about how that really is going to work?

What happened with the Exim, with the mixed credit program that was aimed at AT&T in Indonesia? How do we get better coordination between the troops? I am concerned that a decision was apparently made by Exim and, as a result, that contract provides for $12 million over the life of the Indonesian commitment for mixed credits. Is that right?

Mr. **Lawson**. Well, it is $12 million from each agency, Mr. Chairman. The U.S component of the $180 million is $60 million, and of the $60 million there is $12 million, $6 million put up by A.I.D. and $6 million put up by Eximbank—I am sorry. Let me see. $12 million and $12 million, for $24 million, excuse me.

Yes, $12 million and $12 million.

Mr. **Obey**. How much does A.I.D. have the authority for?

Mr. **Brown**. $12 million.

Mr. **Lawson**. $12 million.

Mr. **Obey**. Annually?

Mr. **Lawson**. No, $12 million over four years.

Mr. **Brown**. $12 million over four years: $2 million this year and no more than $5 million in future years because there is a cap of $5 million.

Mr. **Obey**. That means everybody else is virtually cut out?

Mr. **Brown**. The amount this year is $2 million, but probably will not happen this year, so up to $5 million is still available for other types of activities.

Referring to the cap on mixed credits of $5 million, we will see whether that cap is still there when next year rolls around.

Mr. **Obey**. So far that is not tied down, is it?

Mr. **Lawson**. No, that is not tied down, because the bid was retendered. President Suharto felt for national interest, as he put it, that the bid needed to be re-tendered, that the two finalists and even the other three countries that were involved in the final shoot-out all had something lacking in their bid and it should be re-tendered.

So we are not going to be in a position to know for six to nine months what the final outcome of that is going to be.

Mr. **Obey**. Was that the problem or were the Japanese just muscling him?

Mr. **Lawson**. Well, I have heard reports.

Mr. **Obey**. What do you think?

Mr. **Lawson**. The Japanese, of course, have vigorously denied that they were using their official development assistance program on this transaction in Indonesia, which is $24 billion a year.

Mr. **Obey**. Do we ever believe a Japanese denial on questions like that?

Mr. **Lawson**. Yes, we do, sir, sometimes.

Mr. **Obey**. What I am getting at is how you intend to use those in the future. What was the total size of the Indonesian contract?

Mr. **Lawson**. The total size of the contract with regard to foreign exchange costs was $180 million, of which Eximbank was supporting $60 million of the U.S. bid by AT&T. There was also a Dutch and Spanish component. AT&T was part of a consortium which also included Dutch and Spanish partners.

Mr. **Obey**. How was the determination made to use the mixed credits in a contract that large, rather than spreading out among a number of smaller possibilities?

Mr. **Lawson**. I think several things. First of all, it was an extremely visible contract in that the opportunity to link with fiber optics the 7,000 islands in Indonesia was something that we wanted our firm to win. So the commercial opportunity was very clear there.

The $180 million was just the tip of the iceberg here, because we are talking about contracts over years of follow-on business that would be billions of dollars.

The second thing is that it was fiercely contended by four other countries and used mixed credit tied aid. We felt that this was a very good case and would help our negotiators in Paris get the attention of our allies if we were to step in—step up to the plate in fact and get AT&T to the table.

Reggie, do you want to add to that?

Mr. **Brown**. Yes. I might add that the developmental implications of the project are great. Indonesia's telephone system is worse than China's. This project would make a significant development contribution to that country.

In fact, for every dollar that the United States put in, $25 was leveraged toward the aid benefit and the overall size of the project. A mixed credit is not antithetical to good development, particularly when it leverages funds to strengthen the overall developmental impact.

Mr. **Obey**. I am not suggesting it is. I am suggesting, or I think Mr. McHugh's concern is, that it can be. It does not have to be, but it can be.

Mr. **Brown**. That is why we feel we have a role to play. If it was left up solely to Exim, I am not sure what kind of developmental impact there would have been.

Mr. **Obey**. I am running out of time. There was something else I wanted to ask you and I have forgotten what it was. I will tell you. I have got three or four other questions here. Let me just submit these for the record or I will be out of time, and simply end it at that.

[The information follows:]

Question: Last year, this Committee was asked to approve a mixed credit program involving A.I.D., Eximbank, and the Trade and Development Program (TDP) that was aimed at making an AT&T telecommunications proposal competitive. This program seemed to illustrate the lack of coordination between our development agency, our export agency, and our TDP program.

If I understand the circumstances correctly, Eximbank initiated the idea, but A.I.D. had never considered telecommunications to be a development priority for Indonesia. Nevertheless, A.I.D. eventually approved the use of the mixed credits program. Unfortunately, TDP has the responsibility for the mixed credit program not A.I.D.—so A.I.D. then had to get TDP to go along with the program. At one time, Eximbank personnel stated that TDP would be providing training funds in the package, but told the Committee that no such commitment had been made.

A.I.D. Response. Please allow me to make just a few comments about your understanding of the circumstances surrounding A.I.D.'s decision to support AT&T's bid for a telecommunications project in Indonesia.

On the contrary, A.I.D. had already made telecommunications a development priority in Indonesia. I recently met with an A.I.D. funded consultant, John Forgrieves, who has worked directly with Indonesia Telecommunications Minister Habibe for some time. Mr. Forgrieves plays a pivotal role in advising Minister Habibe on Indonesian telecommunications development plans.

Before proceeding with the mixed credit for AT&T, A.I.D.'s legal office advised that we still have the authority to do mixed credits.

Finally, it is our understanding that no training funds were provided by TDP and that the issue may have become moot when AT&T, as part of its bid package, promised to move its regional training center from Singapore to Indonesia if awarded the contract.

Question. What mechanisms have been put in place to improve agency cooperation and coordination of the mixed credit area?

A.I.D. Response. I believe the EPC recommendations to Congress on mixed credits have led to greater cooperation among the agencies involved.

Agency to agency consultations are frequent and meetings of the EPC working group on mixed credits are held regularly, keeping all players fully apprised.

Question. What is A.I.D. doing to notify our export agencies of opportunities for U.S. exporters related to our foreign assistance programs?

A.I.D. Response. A.I.D. officers in the field work closely with their counterparts in the Foreign Commercial Service and State Department to ensure that export opportunities are passed along. Certainly, A.I.D. with its "Buy American" requirement generates many of its own export opportunities. Bids to provide goods and services are routinely advertised in the Commerce Business Daily to notify the U.S. exporting community of A.I.D. procurement.

Question. The Administration has stated that there will be a cooperative effort between Eximbank and A.I.D. to combat the unfair practice of mixed credits from the European countries and Japan. What is the mechanism of this cooperation and is it adequate?

A.I.D. Response. As a follow-up to the Administration's recommendations to Congress on mixed credits, A.I.D. and Eximbank have been exploring areas of cooperation. Specifically, we have been exploring the possibility of A.I.D. and Eximbank joint programming of "War Chest" monies. The major benefit of this approach is that A.I.D. could apply development criteria to the selection of projects supported with "War Chest" funds to ensure high development impact. Eximbank does not have field resources and A.I.D. can play a key role in the project identification and vetting process to ensure that we get maximum development leverage from the "War Chest" grant monies.

OPPORTUNITIES IN EASTERN EUROPE

Mr. OBEY. On Eastern Europe, what would we have to provide each of you to assure that no opportunities in this fiscal year would be missed?

Mr. LAWSON. Mr. Chairman, that is just simply an impossible question for me to answer.

Mr. OBEY. I realize that is not a question that you are supposed to answer willingly, because you are here defending the Administration's position. Nonetheless, recognizing that, I am simply asking you, because you will be back again next year. Is the Senate out of line in going as high as they are going? At what level could we be sure no opportunities in Eastern Europe would be turned down by any of you come the end of the fiscal year?

Mr. LAWSON. Well again, I am going to have to beg off on that, Mr. Chairman, from the standpoint that it is very hard to predict the level of business there. You know the difficulties of doing business in Eastern Europe. Our companies have not been in there. There are longstanding supplier relationships that have gone on with Western European firms and Eastern Europe firms the last 20 or 30 years or so.

Their accounting system, their legal system, their banking system, is antiquated and is not westernized. Eximbank sent our team over there last winter and they visited four countries in Central Europe, they visited with the banks, which is of course the way that we normally carry out our program. And the banking systems do not have a record of doing any credit analysis.

So it is extremely difficult to know just how we go about doing business. We are eager to do it, we want to do it. We want to support the U.S. exporter and we want basically to support these fledgling democracies. This is the time to support them, not later on.

But having said that, U.S. business people have pointed out to us time and time again that it is very difficult just to find who is speaking with authority in any given agency in Eastern Europe right now, because the focus of power is shifting so radically from state and party down to other groups that have not even been defined yet.

So I just have to beg off on that if I may, Mr. Chairman. It is very hard for me to put a figure on it.

Mrs. RABB-AYRES. Mr. Chairman, I also could not give you an exact figure. When you ask how much could we use so that no opportunities are turned down, there are a range of opportunities. Some are far more valid than other opportunities.

I think that if any of the agencies here are given additional funding, then that does give us a great deal more flexibility. But in terms of how much we would need or how much we could use in a very effective way in this fiscal year, again it is a bit difficult because we are talking about having in the case of TDP a grant in place before the end of September.

I have no doubt that we could have a good deal more in terms of grants by the end of September. But it is probably more realistic to give a little bit more time and actually go into the next fiscal year, because we do not control the timing on the side of the Hungarians or the Poles.

Mr. OBEY. That is, frankly, my preference. The problem is that there is going to be such a squeeze in the next fiscal year. There is a train moving now. So the question is when do you take advantage of the opportunity?

Mrs. RABB-AYRES. Well, certainly it would be extremely helpful if, as in the SEED–1 funds, the funds were no-year funds so that we could have something in place, but not be bound by having the grant actually signed the last day of September, because in the case of TDP if we do not spend those funds by the last day of September we lose them.

Given the fact that we do have to wait on the approval and the signing of other governments, and given the fact also that it is likely that Czechoslovakia will open up and we have not yet gotten into Czechoslovakia, we could have——

Mr. OBEY. Did we not give you two-year money?

Mrs. RABB-AYRES. Yes, the SEED money is available beyond September. But not the rest. The rest of our budget is not. But the SEED money, the $2 million for Hungary and Poland, yes. And that is very useful, but I do expect that we will spend that in this fiscal year.

Mr. BERG. Mr. Chairman, beyond what we think we can provide for Eastern Europe, over and above the $40 million that was earmarked by Congress for Poland, we have another $15 million to $20 million in IG projects under consideration given the size of our project pipeline. Obviously, what we will do is pace ourselves so we can maximize our participation in in those projects.

I would also say that, in light of the question I think you are asking, which, if I understand it, was about taking 1990 money away from Panama and Nicaragua and giving it to Eastern Europe and asking what would that mean, OPIC is planning to be able to actively serve both of those areas. So, I think funding that comes to OPIC, investment guarantee authority, could go either to Eastern Europe or to the new opportunities in Central America, and what we do not do in one region we could do in the other. In some cases there is a timing factor.

Mr. OBEY. My honest view is that it regards to Panama and Nicaragua, I think the Administration arrived at a figure pulling it out of the air.

Mr. BERG. You mean in the supplemental?

Mr. OBEY. Yes. So I do not know the level we really need to provide there. I do not think the Administration does, either. So I am simply looking for the right balance.

How much more would this committee have to provide for Eastern Europe before the Administration responded by saying, "that is ridiculous"?

ASSISTANCE TO EASTERN EUROPE

Mr. BROWN. Mr. Chairman, if I might add another perspective to this issue, since you are talking about the relationship between Eastern Europe and Panama and my agency is involved. I believe you are aware that not long ago Deputy Secretary Eagleburger presented some numbers on the U.S. assistance package for Eastern Europe. The count I have before me, totals $1.9 billion in 1990, when you count debt rescheduling. Over the two-year period the authorized amount is $4.1 billion, again counting debt rescheduling, which is a significant part of the package. When you take into consideration the fact that 18 countries have offered more than $14 billion in credit and grants to Poland, we are looking at a pretty substantial program there.

Mr. OBEY. I am having a terrible time tieing these numbers down, because when we were at the White House yesterday I heard numbers that were very different from that.

Mr. BROWN. Well, if you count the debt rescheduling, which is significant, it is over a billion dollars in 1990, and almost $2 billion if all U.S. government activities are included. Debt rescheduling changes the picture quite a bit, but we think it has to be taken into account.

Mr. OBEY. Well, my question to you is, since I heard a quite different figure when we were at the White House, what is your understanding of how much has been made available from all sources to Poland for this year?

Mr. BROWN. The total SEED package for Poland and Hungary totals $604 million appropriated for FY 1990.

Mr. **Obey**. I thought you just said $14 billion.

Mr. **Brown**. I am coming to that. The $604 million U.S. package includes the structural adjustment funds, including agricultural commodities at $325 million; private sector development, at a little over $55 million, which includes the enterprise funds; the trade credit insurance program, at $200 million; the TDP program at $4 million; educational and cultural activities, $7 million; other SEED-related activities, democratic institutions and what have you, a little under $20 million.

And then we get into other U.S. government activities.

Mr. **Obey**. I have got our list. What I am looking for is from all sources.

Mr. **Brown**. Including all sources, my tally is $1.94 billion, which includes one billion dollars of debt rescheduling.

Mr. **Obey**. No, no, you are focusing on Uncle Sam.

Mr. **Brown**. Funds from U.S. Government Agencies yes.

Mr. **Obey**. I am asking you about the whole world.

Mr. **Brown**. I'm sorry.

Mr. **Obey**. What are we talking about?

Mr. **Brown**. My tally on all donors is roughly $14 billion. I do not have the numbers on the country by country breakdown in front of me.

Mr. **Obey**. We were told at the White House yesterday the figure is $21 billion.

Mr. **Brown**. Well, that is an even bigger estimate, but we do know that it is at least $14 billion.

Mr. **Obey**. My point is that when I hear two very big numbers like that I am forced to conclude they are pulling all of them out of the air. My question is, how in the hell can we make some determinations when the Administration is giving us a number within a one-day period that varies by 50 percent?

Mr. **Brown**. I can show you how I got the $14 billion.

Mr. **Obey**. Since we are supposed to mark up something by the end of this week, it would be helpful—and I know you do not have the full load responsibility for this——

Mr. **Brown**. That is the Secretary of State's responsibility.

Mr. **Obey**. I am not chewing on you. But I would like to have somebody give me a number which the Administration agrees upon for assistance into each of these countries this year from all sources.

[The information follows:]

G–24 ASSISTANCE TO POLAND AND HUNGARY (PLEDGES AS OF 2/20/90) AND PARIS CLUB RESCHEDULING

[Dollars in millions]

	Food aid	Tech/voc	Investment/ trade credits	Environment	Other	Stability fund	Total
Australia	4.2	0	0	0	0	0.8	5.0
Austria	3.4	21.0	496.8	0	0	20.0	541.2
Belgium	0	0	166.7	0	3.6	0	170.3
Canada	11.0	9.2	18.5	0	14.0	25.0	77.8
Denmark	0	0	195.0	10.3	0	0	205.3
FRG	0	6.8	3,205.8	0	849.1	250.0	4,311.8
Finland	8.4	.5	102.0	10.3	0	5.1	126.3

G–24 ASSISTANCE TO POLAND AND HUNGARY (PLEDGES AS OF 2/20/90) AND PARIS CLUB RESCHEDULING—Continued

[Dollars in millions]

	Food aid	Tech/voc	Investment/ trade credits	Environment	Other	Stability fund	Total
France	0	17.3	748.8	0	0	100.0	866.1
Iceland	.4	0	0	10.3	0	.3	11.0
Ireland	0	0	0	0	1.0	0	1.
Italy	96.0	1.6	616.0	0	168.0	100.0	981.6
Japan	27.0	27.0	1,814.8	0	0	150.0	2,018.8
Luxembourg	0	0	0	0	.6	0	.6
Netherlands	0	3.1	0	0	13.1	0	16.2
New Zealand	0	.1	60.0	.1	.3	0	60.5
Norway	7.9	1.5	47.5	11.9	0	5.0	73.8
Portugal	0	0	0	0	0	2.5	2.5
Spain	0	1.2	52.8	0	0	14.0	68.0
Sweden	0	0	153.0	61.3	115.2	10.6	340.1
Switzerland	3.4	3.4	107.3	20.2	0	30.0	164.2
Turkey	1.1	.6	217.1	0	.2	1.5	220.6
United Kingdom	0	152.5	25.2	0	0	100.0	277.7
United States	144.0	60.0	510.7	44.2	42.6	200.0	1,001.4
EEC	150.0	0	1,560.0	0	0	0	1,710.0
EIB	0	0	1,200.0	0	0	0	1,200.0
Subtotal	456.7	305.9	11,298.0	168.5	1,207.8	1,014.7	14,451.7
Paris Club rescheduling by official creditors							9,400.0
Total							23,851.7

Source: European Commission for data on G–24 assistance.

INVESTMENT OPPORTUNITIES IN POLAND

Mr. Obey. This leads me to my last question. I am concerned that given the greater absorptive or, let us say, the greater enticement power of countries like Hungary and Czechoslovakia as opposed to Poland, I am concerned that Poland will not have sufficient attention paid to it in terms of investment opportunities or other help.

In my view, the most important question in Eastern Europe is on what happens to the Poles and the implications that has for Soviet reform. What suggestions would you have that we could take into account in trying to assure that we are providing the specialized attention Poland needs so it will not be overlooked? If things were looked at on a level playing field, investment opportunities might be greater elsewhere in Eastern Europe rather than Poland.

Mr. Lawson. We should have a chance for everybody to answer that question.

Poland is, of course, a crucial player. It is by far the largest country in Central Europe. It seems to me that, as I mentioned in a previous statement, that what the Poles need most of all, beside the short-term insurance that we are offering on both the TCIP and what the Bank is offering, too, for both public and private sector that goes beyond the TCIP—is the medium-term.

This is what the Bank is looking at right now, and then we hit up against this medium-term ceiling that you and I have discussed here of $215 million. And one of the things that would help Eximbank, Mr. Chairman, would be to remove that ceiling so we can get at more medium-term credit for Poland.

We have not yet made the determination to go on cover medium-term in Poland. That still has to be made, and within that consideration goes an awful lot of credit analysis considerations. But the best thing that could help the Bank would be the removal of that medium-term cap.

Mrs. **Rabb-Ayres**. Mr. Chairman, frankly, it has not been my experience that Hungary and Czechoslovakia would outpace interest that is already in Poland. In fact, with what we are doing we are looking at a number of projects in Poland. We are spending a great deal of time on Poland.

Of course, we have not yet investigated the opportunities of Czechoslovakia. But the political situation right now in Hungary makes it very difficult for decisions to be made. And while there are tremendous frustrations doing business in Poland, we know that with a bit of patience we can really make a difference. And certainly the desire on the part of the Polish authorities matches the very, very strong desire that we see on the part of the U.S. business community to do business in Poland.

So I think that it is more an issue of how much we can accomplish. I do not think that we would require any kind of specific—we would not require specific guidelines to insist that we operate in Poland. I expect that we are going to be spending a good deal of time and money there.

Mr. **Berg**. I would say we see a project pipeline for United States private investment in Poland that is going to mature, probably not in this fiscal year but into 1991 and even beyond. This is particularly true for small and medium-sized companies who will invest there.

There is a real lack of information in the American investment community about Poland, but a real desire to invest over there for good commercial reasons and for non-commercial reasons.

What we are doing with our 1990 resources, particularly the $40 million that is earmarked for Poland, is we are investing it, if you will, into a project that will be there to help to finance projects into 1991 and beyond, the Eastern Europe Growth Fund. We are also hoping to create this year some small loan facilities to catch the beginnings of the project pipeline.

We are using IG money and IG authority that was set and designed by all of us for 1990 at a time when we did not anticipate the re-emerging democracies in Central America. By earmarking so much of our IG authority for Eastern Europe to invest it to be able to serve investment in the future, we do see a challenge with regard to what we can do in Central America now.

Again, I would say that for us there is a direct link there. That is why we are talking with State and OMB about what can be done with investment missions and other programs even within the current 1990 period, and certainly 1991, to position us to support American investment.

But I think right now we are investing in order to serve a later-maturing project pipeline, for Poland particularly.

[The following was provided for the record:]

OVERSEAS PRIVATE INVESTMENT CORPORATION
WASHINGTON, D.C. 20527, U.S.A.

OFFICE OF THE
PRESIDENT

March 21, 1990

Honorable David R. Obey
Chairman, Subcommittee on Foreign Operations
Committee on Appropriations
House of Representatives
Washington, D.C. 20515

Dear Mr. Chairman:

Thank you for the opportunity to testify today before your subcommittee on the question of FY 1991 limitations on the OPIC Investment Guarantee and Direct Investment Fund programs.

During the question period, you asked about the effect of a shift in resources from the President's recent supplemental appropriations request for Panama and Nicaragua in favor of additional funding for Eastern Europe, particularly Poland. I responded that insofar as OPIC is concerned, such a shift would not better position us to fulfill our mandates. Our project pipeline for Eastern Europe, especially Poland, will mature in FY 1991 and beyond. We therefore intend to invest in that pipeline to the limit of our available FY 1990 IG authority of $40 million (for Poland) by capitalizing an Eastern European Growth Fund. We will use additional FY 1990 IG and DIF authority for specific project finance in Poland and Hungary while also meeting demand in other parts of the world. OPIC believes that the President's supplemental request for Panama and Nicaragua is needed for the serious economic recovery challenges in those countries. Stated differently, OPIC has sufficient IG and DIF resources in FY 1990 to meet FY 1990 Eastern Europe project demand.

I want to emphasize OPIC's position on these issues in order to underscore the fact that we will commit our entire FY 1990 IG and DIF authorities in a manner that positions us to serve a later maturing project pipeline and serve current needs.

Sincerely,

James D. Berg
Executive Vice President

EXIMBANK FY91 FUNDING

Mr. **Obey**. Well, I think the only observation I would have in closing is that with the $400 million that you indicated would be available in Panama for Exim opportunities and $70 million that you mentioned——

Mr. **Berg**. Panama?

Mr. **Obey**. I am talking about Panama.

Mr. **Berg**. Okay, yes.

Mr. **Obey**. The Administration not requesting any additional funding next year for the Eximbank seems to me a bit out of sync. I know that is not your responsibility, but it seems short-sighted nonetheless to me.

Thank you all for coming. I appreciate it.

Questions for the Record from Mr. Obey

SUBMITTED TO AGENCY FOR INTERNATIONAL DEVELOPMENT

CAPITAL PROJECTS

Question. What does A.I.D. presently think about the share of its spending devoted to capital projects? Is there any consideration within the agency for expanding programs in this area? How would A.I.D. have to change, if at all, to place more emphasis on economic infrastructure activities? In what areas would A.I.D. cut back in order to accommodate an expanding share for capital projects? Which aid recipients would likely benefit the most from this type of shift in U.S. policy?

Answer. The total amount of our program devoted to capital projects is very small—less than 4 percent.

Yes, there is some consideration being given to A.I.D.'s capital projects program. A.I.D. received a mandate from the Economic Policy Council (EPC) of the Cabinet in September 1989 to see if it could do more in the capital projects area in support of our negotiations to eliminate mixed credits at the Organization for Economic Cooperation and Development in Paris.

I do not anticipate that any changes would have to be made to existing A.I.D. programs, given our long association with capital projects development and our ongoing efforts in this area. Any expanded capital projects program would have to be done within our budgetary constraints and under current authorities for existing programs.

I do not foresee any cutbacks to accommodate more capital projects since I do not see them as inconsistent with A.I.D.'s current development strategy or programs in a whole host of areas.

The most likely beneficiaries of more capital projects would be the "spoiled markets" of the Pacific Rim and North Africa. These countries were targeted by the September 1989 EPC recommendations to Congress on mixed credits. A.I.D. will do what it can, within existing budgetary constraints, to support the Administration position in these countries. However, other areas of the world are not out of the question. For example, A.I.D. has supported over $150 million worth of transportation projects in Southern Africa.

A.I.D. CONTRIBUTION TO U.S. ECONOMIC INTERESTS

Question. How do you think A.I.D. best contributes to American economic interests? What more could it do without compromising the mandate of the agency? A.I.D. officials often state that roughly 70 percent of all economic assistance funds are spent in the United States. Can you briefly outline the methodology used to arrive at that figure? Is this still a valid figure? Specifically, how do you account for the large cash component of U.S. aid and what part of it is spent in the United States?

Answer. A.I.D. best promotes U.S. economic interests through policy reform programs where we seek to promote free market principles and to persuade and assist developing countries to open their trade and investment regimes. And because trade and investment is a two-way process it helps stimulate economic growth in developing countries.

The Foreign Assistance Act assures direct benefits to the U.S. taxpayer by providing generally that purchases of goods and services with A.I.D. funds be made in the U.S. ESF project assistance and commodity import programs prescribe U.S. procurement. Of course our food aid program is tied and 75 percent of the shipment of these commodities is on U.S. shipping lines.

I am aware of the 70 percent estimate and that's what it is—an estimate. We are investigating how we can improve the calculation of this estimate and ensure that adequate data is being collected.

At this time I am not sure that the 70 percent estimate is a valid figure and that is why we are taking another look at it.

It is my understanding that A.I.D. receives assurances from all cash transfer recipients under the ESF program that an amount of eligible goods and services at least equivalent to the value of the cash transfer will be imported from the U.S. Because ESF funds are provided to achieve overall U.S. foreign policy interests, there have been certain exceptions made to the general practice; mentioned above.

Recently, ESF cash transfer resources have been used in selected countries for payment of host country debt to international institutions or to the U.S. in support of multi-donor financed economic adjustment programs.

TIED AID

Question. What is A.I.D.'s current policy regarding tied aid? According to some figures, the American aid program is less-tied than many other major donors, such as France, West Germany, and the U.K. What has been A.I.D.'s position on tied aid during donor coordination meetings; are we pressing other countries to untie their assistance? Are there pressures on the Agency to increase the level of tied aid? Japan claims to have the most untied aid program—what is your assessment?

Answer. Except for the Development Fund for Africa (DFA), A.I.D. is required by law to limit its procurement to the U.S., developing countries and in exceptional cases, free world industrialized countries. The food aid program is the most tied and our ESF project assistance and commodity import programs are also tied to U.S. procurement. Although the DFA is exempt from procurement tying as a matter of law, U.S. procurement is maximized as a matter of policy. Cash transfers under the ESF program for balance of payments provide free foreign exchange.

A.I.D. is opposed to the use of mixed credits. However, A.I.D. is implementing the EPC's recommendations to Congress on pursuing a more proactive approach in the use of mixed credits. This policy is intended to support our negotiations at OECD, aimed at the eventual elimination of mixed credits.

I am not aware of the data you refer to but guess that it comes from the Development Assistance Committee of the OECD. If so, we should exercise some caution here.

The multilateral character of the DAC makes accurate and reliable data collection and reporting extremely difficult and a cumbersome issue to negotiate. We frankly do not think the data is very good and are trying to fix that. An upcoming meeting of the DAC will address the data issue and we expect to try to make the data more comparable and useful to all donors.

We are skeptical about the Japanese having the least tied program. Many components of their program are very opaque. We have been discussing with them the possibility of providing us with data on a project by project basis, which will better show procurement outcomes. I believe a recent study team sent out by the GAO expressed similar reservations about the untied nature of the Japanese program.

U.S. PARTICIPATION IN JAPANESE AID PROGRAM

Mr. OBEY. Over the past year or so, a small unit in A.I.D. has been attempting to establish better links with Japan's aid program in the hopes of gaining greater American participation in Japanese aid project procurement. Last year A.I.D., with the support of Japan's Foreign Ministry, held two workshops for U.S. businesses and consultants intended to explain the Japanese aid system and how Americans might participate. A follow-on conference is scheduled for September in Tokyo. How successful has A.I.D. been in opening the Japanese aid program to American participation? Are you going to continue these efforts in the future? According to the Japanese statistics, West European interests have been far more successful than U.S. firms in gaining procurement contracts from Japanese aid. Why do you think this is the case? What can A.I.D. or American business do to reverse this trend?

Answer. As you indicated the unit responsible for this endeavor in A.I.D. is very small and it has accomplished quite a lot with a staff of three people. However, I believe it is still too early to gauge the concrete results of their effort to make U.S.

businesses aware of the Japanese aid program and what successes may have been achieved by U.S. companies to sell goods or provide services under the Japanese aid program.

It is unclear whether we will be continuing these efforts in the future. I believe some evaluation of its success must be made before we proceed further.

Besides, as I indicated earlier we still need some very basic data before we can accurately assess just how untied the Japanese program is.

Concerning the issue of more European procurement being done under the Japanese program, I really have no comment since we have not seen sufficient data on this issue to make a judgment.

SUBMITTED TO EXPORT-IMPORT BANK

EXIMBANK INVOLVEMENT IN EASTERN EUROPE

Question. The shake-up of the political structure in Eastern European countries has increased the potential for a sharply expanded role for U.S. businesses and exporters in those countries. These countries face considerable obstacles in reinvigorating their economies, during which time they will need, and likely ask for, broadly expanded trade credits and assistance from the United States and other Western countries.

What is the status of the Bank's involvement with each of the countries in Eastern Europe? What conditions would have to be met before the Bank would consider upgrading its involvement in, or in changing the status of the countries in Eastern Europe?

Assuming the Jackson-Vanik and Stevenson amendment waivers were granted and the countries in Eastern Europe were removed from the list of Marxist-Leninist countries, American companies may significantly increase their commercial activities in Eastern Europe. Has the Bank made an assessment of the kinds and extent of credits and/or guarantees that would be requested by U.S. companies?

Answer. The Bank is presently open under all of our programs in Hungary, Yugoslavia and Czechoslovakia. Eximbank's current exposure in Hungary and Yugoslavia is $3.2 million and $1.15 billion, respectively. The Bank has just recently opened in Czechoslovakia.

With respect to Poland, Eximbank is open under our short-term insurance program to public and private sector buyers. The Bank's insurance program complements A.I.D.'s $200 million TCIP program for private sector buyers, which is in the final stage of implementation.

Eximbank is legislatively prohibited under the Jackson-Vanik Amendment of the Trade Act of 1974 and Section 2(b)(2) of our legislation from providing financing assistance to the U.S.S.R., Bulgaria, Albania, and East Germany. In order for the Bank to open in these markets, the President would have to waive the Jackson-Vanik Amendment and determine that it is in the U.S. national interest for the Bank to do business.

With regard to Romania, the Bank stopped providing financing support to this market in 1988 when Romania renounced MFN treatment, Therefore, in order for the Bank to open in this market the President would have to extend a waiver under the Jackson-Vanik amendment.

At such time as these legislative prohibitions are waived or lifted, the Bank will determine the parameters of our programs. However, the Bank has never been open in Bulgaria, East Germany or Albania so the extent of our possible involvement in these markets is unclear.

At this time, it is very difficult to predict what the specific demand on our direct credit or guarantee resources from Eastern Europe will be for FY'90–91. We have estimated some $300 to $500 million in demand for Eastern Europe under all of our direct loan, guarantee and insurance programs starting in FY'91. The Bank has made or is making preliminary commitment offers on three large Hungarian transactions which total $152 million. These offers all concern projects that are subject to international competitive bidding. The other competing bidders are all European suppliers with an established presence in Hungary and the other Eastern European countries. We do not know how long it will take for the purchasers to award these contracts, or when these contracts are awarded whether the purchasers will use official export financing or private sources. Furthermore, we do not know if the Bank will become involved or whether our involvement would be in the form of a loan or a guarantee.

We believe that major or extensive new capital projects are unlikely to proceed until newly elected governments are firmly established and, following that, until project needs are reevaluated. Those governments that have made the most progress toward these goals can be anticipated to move with greater speed into credit markets. Moreover, those countries with the greatest orientation towards a market economy will be able to move with the greatest ease in using their credits. In addition, bidding, bid evaluations, and contract negotiation will take up a further period of time. Thus, any significant demand for Eximbank financing assistance will inevitably take a certain length of time to develop into specific requests for final commitments of our loan or guarantee authority.

EXIMBANK'S DIRECT LENDING PROGRAM

Question. The direct lending program of the Export-Import Bank was established to provide assistance to U.S. exporters facing foreign officially subsidized credit competition. From FY81 to FY91, the direct lending appropriation limit declined from $5,461 million to $500 million.

Some critics argue that the reductions in the appropriation level for direct lending have effectively eliminated direct lending as an important program in the Bank and as a credible counterpart to the practices or other governments. Does Eximbank agree with this assessment?

Answer. Over the decade of the 80's annual long-term Official Export Credit Agency activity by all OECD countries declined by some 60–70%, largely in response to the impact of the debt crisis on LDC growth and investment as well as negotiating successes within the OECD which removed the subsidy from whole categories of buyers (e.g., rich countries) and sectors (e.g., aircraft). Eximbank activity was particularly impacted by these developments, but it has had little adverse impact on the demand for mixed credits, which has been one of the key areas of EXA demand in the 80's. Moreover, Exim has remained a significant player in its traditional markets of Latin America, Asia and Africa. For example, in the early 80's, Eximbank accounted for 10–12% of OECD long-term activity; in the later years 6–9%. Excluding the effect of aircraft, the size of Exim's role in the later years closely approximates the early 80's.

EXIMBANK'S TIED AID CREDIT PROGRAM

Question. In March 1987 the participants to the Arrangement on Guidelines for Officially Supported Export Credits negotiated a new tied aid credit agreement which was fully implemented in July 1988. Congress also established a tied aid credit fund in Eximbank to counter the use of predatory tied aid credits by other OECD (Organization for Economic Cooperation and Development) countries.

How have the participants to the Arrangement lived up to its terms? Specifically, has the Arrangement caused other countries to reduce the size of their tied aid credit program?

Answer. In July 1987, the Participants in the Arrangement implemented new rules governing the extension of tied aid credits. The key changes include: (1) the establishment of a prior notification period, the purpose of which is to make more transparent the availability of tied aid and to give those countries who wish to match these credits the opportunity to do so; and (2) an increase in the minimum permissible concessionality level from 25% to 35%, thereby increasing the cost of providing such support. With few exceptions, these rules are observed by the participants.

Nevertheless, the desired effect of the new rules has not been realized. Although the increase in the minimum concessionality level did increase the cost of providing tied aid, it has not proven to be a deterrent to the incidence of such support. Donor countries have either increased their tied aid budgets to accommodate the required higher levels of concessionality, or reduced the average concessionality level in tied aid offers, thereby spreading the same amount of aid resources over the same (or an expanded) number of recipients. Hence in November 1989, the U.S. initiated a new round of negotiations in the OECD to address the tied aid credit issues.

Question. Which countries are the most aggressive in using tied aid credits; which areas of the world are they the most active, and what effect have their activities had on U.S. exporters?

Answer. In April 1989, an interagency report was submitted to the Congess by Eximbank entitled 'Report to the U.S. Congress on Tied Aid Credit Practices". A key finding of the study was that U.S. exports on the other of $400–$800 million are lost annually as a result of other countries' tied aid credit practices. The markets in which U.S. sales were most adversely affected include Asia (notably India, Indonesia, Thailand, and at the time China), North Africa, the Middle East and to a lesser extent, Latin America. While most industrialized countries sponsor a commercially-motivated tied aid credit program, except for the United States, the primary donor countries include Japan, France, the U.K., Germany, Italy and Canada. Each of these countries continues to use its tied aid program aggressively, depending on the market or sector of sale.

EXIMBANK'S FINANCIAL CONDITION

Question. Since the early 1980's, the Export-Import Bank has suffered a substantial erosion in its capital base. For instance, in FY81 the Bank's equity was $3.2 billion; by FY91, estimates indicate that the Bank's equity will be in deficit by $4.5 billion—a loss of $7.7 billion in 10 years.

Despite the erosion in the Bank's capital base, the Bank has not asked for a capital replenishment, but has argued that its fortunes can be improved if it can make new loans at rates that are above the Bank's costs. Is the Bank able to make new loans at rates that are above its costs? What is the average interest rate spread between the rate at which the Bank obtain its funds and the rates at which it makes its loans? When does the Bank estimate its equity will be in a positive position.

Answer. Interest and fees charged on new loans that have been made by the Bank could well be adequate to cover our costs of borrowing. For new loans authorized in FY 1989 and FY 1990 through March 31, the weighted average interest rate was 8.34% and 8.04%, respectively. The weighted average rate on new borrowings in the same time period was 8.91% and 8.19%. Including the commitment fee of .5% on the undisbursed balance raises the yield on new credits sufficiently to cover the cost of borrowing at this time.

However, the Bank's equity position will remain negative for the foreseeable future. But, there is no need for a capital infusion in order for the Bank to continue to operate since the Bank has the backing of the full faith and credit of the U.S. Government. Thus, the Bank can continue to borrow to fund its operations regardless of its capital position.

DIRECT LOAN PROGRAM

Question. In the mix of the Bank's programs, what is the importance of the direct loan program vis-a-vis the guarantee and insurance program to the exporter especially in times of rising interest rates?

Answer. The purpose of the direct loan program is to enable the U.S. to neutralize the influence of foreign official export credit subsidies on buyer decisions, and the purpose of guarantees and insurance is to offset the frequently exaggerated perceptions of foreign risk as well as maturity and floating rate risks. Given the volatile relationships among the economies and interest rate levels of the major countries, there are times when the market rates provided under an Eximbank guarantee are competitive with the rates an Eximbank credit would be allowed to charge under the OECD interest rate matrix. However, during periods of rising U.S. interest rates a guarantee is less competitive than a direct loan commitment.

Question. Has the Bank's aggressive use of the War Chest, since it is a subset of the direct loan program, put undue pressure on that program to fund normal business activity? What operational activity has the Bank had to employ to cover outstanding bids (such as holding back using authority in order to carry-over and cover projects into the next fiscal year)?

Answer. The Administration has initiated a policy of aggressive use of the War Chest. This will increase the use of the War Chest and leave less authority for other direct credits. This may result in the Bank having to defer into the next fiscal year loans which otherwise would have been authorized this year. However, to date the Bank has not had to hold back using loan authority in order to commit War Chest grants.

FUNDING TRADE PROGRAMS

Question. From a policy standpoint, how does the Administration reconcile the apparent contradiction between declaring that (quote, Eagleburger)

"we are going to have to acknowledge that our economic health and our ability to trade competitively on the world market may be the single most important component of our national security . . ." and then turning around and opposing reductions in both Eximbank and TDP from the current fiscal year level?

Answer. The reductions in Eximbank and TDP are small parts of a large deficit reduction package whose benefits to the vitality of the overall economy and competitiveness of the export sector are much more significant than any incremental changes in individual programs.

LOAN LOSS RESERVE/FINANCIAL CONDITION

Question. Now that Exim has created a loan loss reserve can we expect that the GAO will issue a clean accounting letter, or are there any other problems?

Answer. The Bank does not intend to request a recapitalization. Even though negative equity will show on the financial statements, this will not prevent the Bank from being able to operate normally. The Bank will be able to continue funding its operations by borrowing from the FFB, regardless of the equity position. If the Bank were to be recapitalized, however, the amount of the loss reserve would have to be taken into account in determining the amount needed for recapitalization.

Question. The Bank is now in a negative asset position. Can you project that the Bank will ever work itself out of this situation?

Answer. The question of whether the Bank can work itself out of its negative equity position depends on several factors. Currently, there is a large non-performing loan balance of approximately $2.5 billion. However, new credits are being made at rates that are close to our cost of funds and with the inclusion of fees, are generating income. If worldwide economic conditions improve so that interest collections resume on some of the non-performing loans, and the spread between our lending and borrowing rates remains favorable, it could be projected that at some point well into the next century we could eventually work out of our negative equity position. However, absent a recapitalization, the Bank's equity will remain negative for the foreseeable future.

Question. What would the effect of forgiving Poland's debt to Exim have on the Bank's balance sheet?—Haven't you already fully reserved for the loss of the old Polish debt?

Answer. Exim's loan loss reserve is not country specific. The reserve is calculated by grouping credits into categories of debt and applying an average reserve percentage to each category. No category is reserved at 100%. Therefore, the forgiveness of all of Poland's debt or the debt of any other country would require an increase to the loss reserve and an additional charge to income.

SUBMITTED TO OVERSEAS PRIVATE INVESTMENT CORPORATION

MARKETS FOR U.S. EXPORTS

Question. How do OPIC projects contribute to the development of new overseas markets for U.S. exports.

Answer. OPIC projects contribute to the development of new overseas markets for U.S. exports in a number of ways. On a very broad level, the ability of the United States to export its goods and services is heavily dependent upon the capacity of other countries to buy those goods. Developing countries represent huge potential markets for U.S. goods, but purchases by many of these nations are constrained by balance of payments difficulties, and low national income levels. By creating jobs, tax revenues and balance of payments savings in developing countries, OPIC-supported overseas investment helps to create growing, prosperous local economies that can absorb U.S. exports.

More directly, U.S.-owned enterprises overseas also stimulate U.S. exports by drawing raw materials, components, equipment and other goods and services from the United States to the overseas plants. U.S. subsidiaries frequently maintain close ties with their parent companies and U.S. suppliers, and look to them first when purchasing necessary capital goods and production inputs. In fact, more than a quarter of all U.S. exports are to overseas subsidiaries and affiliates of American corporations. Additionally, overseas plants open new export opportunities for other U.S. produced goods, as distribution channels are established and local consumers become familiar with American products, quality and standards.

Almost any type of project which OPIC supports may generate demand for U.S. export. Manufacturing projects may purchase capital equipment, spare parts, and other raw materials from the United States. Mining projects frequently make heavy use of U.S. mining, drilling and other equipment. Many food processing projects utilize U.S. agricultural products—for example, an OPIC-supported animal feed mill will stimulate the export of U.S. grown wheat, corn and other grains. Also—perhaps suprisingly—many service projects support and stimulate U.S. exports. OPIC has assisted a number of distributors of U.S. produced machinery and equipment, including a construction equipment distributor in Bolivia and a machine tool accessories distributor in Korea. Repair and servicing facilities can also help stimulate U.S. exports since the availability of service is often weighed heavily in the product buying decision. For example, an OPIC-assisted tractor service and repair facility in Egypt will help U.S. produced tractors compete successfully in the Egyptian markets.

OPIC also has two specialized programs which provide strong support to U.S. exports. OPIC's Contractors and Exporters program gives suppliers of U.S. goods and services to overseas markets protection against political risks. Many U.S. machinery and equipment exports have been facilitated by this program, including the export of spraying equipment, hot air fired biomass engines, drilling and seismic exploration equipment, generators, helicopters and laboratory equipment.

OPIC's leasing program also stimulates U.S. exports. Although the ownership of the machinery and equipment leased to foreign countries remains in the United States, most leased equipment remains overseas throughout its useful life, and therefore constitutes a U.S. export. OPIC has supported many leasing projects over the years, including the lease of planes geothermal drilling equipment and tunneling equipment.

The volume of U.S. exports directly stimulated by OPIC-supported projects bears testimony to the benefits accrued by U.S. exporters from overseas investment. Initial exports of U.S. machinery, equipment and supplies to the 123 projects assisted by OPIC in FY 1989 are valued at $739 million, while operational procurement from U.S. sources will generate another $1.5 billion during the first five years of project operations. Less measurable are the effects on U.S. exports of the strengthening of developing economies and increased consumer familiarity with U.S. brands. Clearly, however, OPIC-supported projects have played an important role in helping to develop markets overseas for U.S. produced goods and services.

EASTERN EUROPE

Question. Has OPIC taken any role in providing U.S. support for the political and economic reforms taking place in Eastern Europe?

Answer. OPIC plays an influential role in supporting the political and economic reforms occurring in Eastern Europe in two ways: directly, through our contacts with representatives of the region's governments and, indirectly, by providing both a forum for and financial assistance to the development of commercial relationships between U.S. businesses and their counterparts in the region.

OPIC utilizes contacts with officials of the region's governments to explain both the philosophical and practical concerns of the American private sector and to help them devise ways in which to respond to those concerns. These discussions occur regularly, and often are initiated by the non-U.S. participants. Such exchanges occur during the negotiation and implementation of our bilateral investment agreements, briefing sessions in which host governments discuss with us their needs, priorities and commercial laws or which OPIC explains the ways in which we can assist host governments and foster U.S. investment in their countries, and government-to-government meetings and mission-related programs convened for the specific purpose of discussing investment barriers and their elimination.

OPIC will support the private commercial sectors emerging in these countries by encouraging U.S. investors to participate in helping them to reach the critical mass and level of productivity they will need in order to be socially and economically profitable. By helping American investors understand the laws and practices in prospective host countries, we increase their comfort level and equip them to make wiser investment decisions. By closely scrutinizing the business plans and financial projections of investors seeking insurance or financial projections of investors seeking insurance or financing, we increases the liklihood that ventures will be well considered and, therefore, successful. Most importantly, OPIC provides the political risk insurance and financing needed to make U.S. investments in Eastern Europe commercially acceptable even during these early stages of the region's economic and political transition.

OPIC play a less direct, but perhaps more pervasive, role in shaping the changes in the region by increasing the contracts between Eastern European business people and their private counterparts in the U.S. Such contacts, whether in the form of questions by an investor learning about their system, expectations of a new American business partner, or introductions to new suppliers, purchasers or competitors, inevitably increase understanding of free-market concepts and structures at work in the United States and provide practical tools with which to construct their own systems.

Question. Why has OPIC decided not to create a "Polish Growth Fund" and instead has worked to create an Eastern European Growth Fund?

Answer. OPIC seeks to support Poland's efforts as it moves toward a democratic form of government and implements free market principles by providing that country with critically-needed financial and technical assistance. However, to make the most effective use of its scrace financial resources, OPIC must develop and implement programs that are responsive to a board spectrum of Eastern European countries. Currently, OPIC is targeting Poland and Hungary; however, under the proposed Eastern European Democracy and Free Market Act of 1990, OPIC would also be authorized to commence operations in Czechoslovakia, the German Democratic Republic, Romania and Bulgaria.

Therefore, the Eastern European Growth Fund is being created with OPIC financial guaranties to raise capital to finance productive business enterprises in Poland as well as other Eastern European nations in which OPIC is authorized to operate. OPIC believes that a broader Fund, as opposed to a narrowly-targeted initiative, will attract more capital from U.S. corporate and institutional investors, partly because a more diversified fund will be perceived as less risky than a single-country fund. At the same time, mindful of Poland's needs, OPIC will ensure that the Eastern European Growth Fund will utilize at least $40 million of its capital to finance projects in Poland.

In addition to this initiative, OPIC is currently working on several projects directed exclusively at Poland. First, OPIC is developing a Small Business Loan Guaranty Program for Poland, which will provide loans in amounts up to $500,000 to investment projects spnsored by U.S. small business investors. Eligible projects will include new ventures or the expansion of existing businesses, and may either be wholly-owned by U.S. companies or joint ventures between Polish and U.S. firms.

Second, in conjunction with CARE, OPIC is developing an indigenous investment fund in Poland, for the purpose of making investments in small and medium-sized businesses. Initial investments will target established private small businesses, small state-owned businesses identified for privatization, and segments of larger state enterprises which may be privatized and operated autonomously.

Finally, it is anticipated that OPIC's Environmental Investment Fund will target Poland, where there is an urgent need for financial assistance for projects that manifest a positive, mutually reinforcing relationship between profitable economic development and protection of the environment. The Environmental Fund will identify, invest in, and support new or expanding Polish businesses which use natural resources on a sustainable basis and otherwise practice sound environmental management.

O.P.I.C. PROGRAM EXPANSION

Question. Does OPIC have sufficient administrative resources to expand its operations in Panama, Nicaragua, and other Eastern European countires?

Answer. OPIC operates in over 115 developing countries, with new countries being added regularly. In just the last six months OPIC began or resumed operation in Poland, Hungary and Panama, all high priority countries for U.S. foreign policy interests. OPIC will shortly begin operation in Nicaragua, another reemerging democracy of special U.S. interest. Private sector investment is very important to support the economic and political reforms taking place in these emerging democracies and other developing countries, a role for which OPIC is uniquely suited. Notwithstanding these additional responsibilities, OPIC operates with a minimal staff of 135 persons, a number equivalent to that at which the agency operated at its inception in 1971, and a modest administrative budget. OPIC resources are sufficient to permit OPIC to carry out its program responsibly. At the same time, we hope to maximize OPIC's developmental and revenue generating activities which in FY 1989 supported $3.3 billion of total investment in developing nations, produced more than $2.2 billion in new U.S. exports (over the first five years of operation), and generated a record net income of $122 million.

PILOT EQUITY PROGRAM

Question. If Congress were to approve funding for OPIC's pilot equity program, what types of business and projects would be supported?

Answer. Equity authority will be used only in those worthwhile projects which would not otherwise go forward because equity financing cannot be arranged and the financial structure of the project will not support the issuance of additional debt. In selecting projects for equity financing, OPIC will give preference to those involving U.S. small businesses or cooperatives. OPIC will also carefully consider the extent to which its equity financing would assist a project sponsor in arranging the entire capital investment required for the project.

Because making investments such as those usually entails greater investor risk than being a secured creditor of a project, OPIC will be very selective in its equity investment program, investing only in those projects with highlty qualified and experienced management, efficient, strongly competitive operations, and established, market-tested products or services.

Potential equity projects have been identified in diverse sectors including agriculture, aquaculture, manufacturing, and forestry. Specific examples of potential equity investments include a Botswana project involving a start-up manufacturer of clay brick and tile products, and the development and operation of a modern shrimp farm in Haiti.

An obvious benefit of the equity program is that it will enhance the competitiveness of U.S. businesses vying for development projects overseas. Businesses are increasingly being required to raise significant equity as well as debt financing for projects on which they are bidding; the availability of such financing becomes an element of the bidding process in which U.S. companies are increasinghly disadventaged relative to competitors from other developed countries.

Questions for the Record from Mr. McHugh

SUBMITTED TO AGENCY FOR INTERNATIONAL DEVELOPMENT

TIED AID CREDITS

Question. What is A.I.D.'s strategy regarding the use of tied aid or mixed credits to assist U.S. businesses obtain overseas contracts, such as we are trying to do in Indonesia with AT&T?

Answer. A.I.D.'s principal objective is development. Collaboration with any public or private source of capital or technology is premissed on its development impact. We do not, therefore, have a strategy for helping U.S. companies like AT&T, but rather focus on how expanded U.S. investment and trade can promote development in any particular aid recipient.

As to tying A.I.D. procurement to U.S. goods and services, our current policy—which you and the other committee members endorsed at the hearing—is to aim at tied procurement. Where this would undermine our paramount development objective, existing regulations allow for a waiver. We greatly appreciate congressional efforts to help assure maximum operational flexibility for the Development Fund For Africa, including the authority to untie A.I.D. funds from U.S. procurement. However, even in this case, we believe the U.S. taxpayer has a right to expect that A.I.D. funds will primarily be used in ways that also help create U.S. jobs. To this end, we are reviewing whether aid programs with a development focus are doing everything possible to protect U.S. jobs.

Question. Given tight resource constraints, why should scarce ESF or DA funds be used for this purpose instead of the EXIM War Chest?

Answer. It is precisely because ESF & DA resources are tight that we have to look for opportunities to leverage them. As a result, we are actively working to co-finance development projects with other bilateral donors, the multilateral development banks, private sources and other official agencies like U.S. Eximbank. This policy reflects the needs of our aid recipients. However, co-financing does not mean that A.I.D. changes its policy direction or project evaluation requirements. In other words, "mixed credits" doesn't necessarily mean "bad development" and where it might, A.I.D. will not be involved.

Question. Does it seem inconsistent to you that on the one hand we are using taxpayer funds in the form of scarce ESF to assist AT&T obtain a telecommunications contract in Indonesia against foreign competitors, including NEC of Japan, while on the other hand AT&T has just entered into a partnership agreement with NEC in telecommunications chips and equipment? Are AT&T and NEC competitors or partners? If they are partners, why should A.I.D. contribute its increasingly scarce assistance to AT&T to secure a contract in Indonesia?

Answer. We are not involved in the details of the commercial agreement between NEC and AT&T which, we understand, has nothing to do with the proposed Indonesian transaction. As you are aware, both these firms are huge industrial enterprises operating in a range of markets and countries. It is not surprising that they may coopeate in one area, particularly where it would enable AT&T greater access to the Japanese market for telecommunications equipment, and compete elsewhere. As you know, the Bush Administration believes that open markets for products and intellectual property is essential to American prosperity.

Question. Conversely, if mixed credits are such good business, financing $24 dollars of project cost and generating $18 dollars of exports for each dollar spent in the AT&T case, why don't we do more of these since they tilt trade in our favor? In the Indonesia case, please explain how you calculated these ratios.

Answer. We would like to do more such projects, but only if they meet development criteria and otherwise contribute to attaining U.S. foreign aid objectives in a particular country. However, the Administration's intent is to not follow the approaches of others, but rather to seek a "level playing field" which benefits developing countries and U.S. businesses.

The methodology for calculating the leverage is straightforward: we compare the amount of ESF financing with the total investment package. The same method is used in calculating the trade ratio by dividing the total projected amount of trade by our ESF contribution. It is worth noting that this formula significantly *understates* the total leveraging of ESF, as it excludes all indirect benefits from this type of transaction such as technology transfer and labor training skills associated with any direct investment project.

An important point is that A.I.D. involvement ensures that Eximbank funds are used to promote development. The Chairman of Eximbank believes this new approach, which is possible only because of A.I.D. involvement, makes good business sense.

Question. There seems to be compelling evidence that using development aid to finance tied-aid credits distorts development aid programs away from real development problems in poor countries to investment opportunities in middle-income developing countries. Does that concern A.I.D. as a development agency?

Answer. There is certainly compelling evidence that donors other than the U.S. focus much of their assistance on developing countries that are important commercial markets for them. But this does not mean that only "middle income" countries benefit, because average levels of national income miss the wide range of individual circumstances and needs.

From the U.S. perspective, assistance comes in the form of Development Assistance, which is primarily focused on development needs, as well as Economic Support Funds which promote both the development and political interests of the U.S. Commercial interests, however, have not been a consideration in the allocation of either ESF or DA.

Question. What is A.I.D.'s legal authority to use development assistance funds and ESF for mixed credits or tied aid?

Answer. The Foreign Assistance Act (FAA) mandates a multi-purpose program of foreign assistance programs and broad range of aid terms and instruments. For example, the existing legal mandate was once used to run a largely loan program and now serves as the base for an almost exclusively grant program. One of the key criteria for any co-financing arrangement is whether the proposed project or program conforms with the FAA objectives. A.I.D. is less concerned with mixed credit financing, but rather focuses on a project's overall economic and social merit. Most important, we look first and foremost to a project or program's development impact and whether its purpose is authorized by the FAA. If it is, and it meets other A.I.D. criteria, the use of mixed credits as a financing mechanism is not proscribed. Excepting the current $5 million cap on ESF used for mixed credits, there is no legislative limit on co-financing through mixed credits.

A.I.D. has, however, chosen to limit its participation in any mixed credit. Existing A.I.D. policy (Policy Determination No. 2, issued in 1982) on the use of development assistance for mixed credits is under review, and no final policy determination has been made. Further, the specific legislative mandates for DA would preclude many of the sorts of projects that might use mixed credits. Given the current FAA wording, we could only finance mixed credits from DA in those sectors authorized by the FAA for development assistance purposes.

SUBMITTED TO TRADE AND DEVELOPMENT PROGRAM

Tied Aid

Question. TDP has been assigned a lead role in administering the tied aid responsibility at State yet it appears the activity is EXIM-AID led. What is your role and is there a teamwork process going on?

Answer. The Omnibus Trade and Competitiveness Act of 1988 amended the Trade and Development Enhancement Act of 1983 (the 1983 Act) to authorize the Director of the Trade and Development Program to carry out a program of tied aid credits for United States exports. The amendments further required the Export-Import Bank of the United States to carry out its program of tied aid credits under the 1983 Act in cooperation with TDP. The Trade Act also provided that ESF may be used by the Director of TDP, with the concurrence of the Secretary of State, to finance tied aid credit activities. However, the Foreign Operations, Export Financing, and Related Programs Appropriations Act 1989, withheld the automatic transfer of ESF to TDP by providing that no ESF appropriated for FY 1988 or FY 1989 were to be made available to TDP for tied aid credits without the additional prior approval of the A.I.D. Administrator. It further limited to not more than $5 million the amount of ESF available to finance such tied aid credits. The 1990 Appropriations Act continued the funding limitation and the requirement for the A.I.D. Administrator's prior approval of the transfer of funds.

In November 1989, the Economic Policy Council of the Cabinet (EPC) approved the recommendations of its Working Group on tied aid credits. The Working Group, chaired by Treasury, consisted of State, Commerce, Eximbank, USTR, A.I.D., TDP, Agriculture, and appropriate representation from the White House. In particular, the EPC approved that Eximbank and A.I.D. should identify possible projects where the War Chest, either alone or in conjunction with A.I.D. bilateral assistance funds, could be utilized. This financing would be used primarily to initiate offers in sectors and markets of interest to U.S. exports where tied aid credits are extensively used, but also to match or overmatch in specific cases to advance negotiations at the OECD. A.I.D. and Eximbank have already cooperated with joint financing to support an American supplier of telecommunications equipment for a significant export opportunity to Indonesia. The form of the funding was a soft loan in which an A.I.D. grant of ESF and War Chest financing were used to buy down the interest rate on a guaranteed loan.

In addition to being represented on the EPC Working Group, TDP attends the weekly Eximbank Board meetings as a means of reviewing proposed mixed credit transactions. TDP also votes on any tied aid credit transactions presented at the NAC for decision.

TDP is also part of the U.S delegation to the Export Credit Working Group of the OECE, which reviews export credit activity under the Arrangement.

As our budget permits, TDP has initiated a program of de minimis tied aid credits in the area of training. TDP has approved eight projects, which in general grant some small amount (3 percent of the contract amount or $1 million, whichever is less) for a training package in support of a U.S. supplier's bid on a contract. For example, the Chilean Telephone Company (CTC) announced an award of a $29 million contract for the construction of Earth satellite stations to the U.S. firm of Scientific Atlanta (SA) after TPD was able to offer a $750,000 training grant to CTC to make SA's bid more competitive. The grant, in conjunction with conventional Eximbank financing and the U.S. Ambassador's support, neutralized strong competition from NEC of Japan and Alcatel of France, and SA was awarded the largest single international contract in the history of the company.

Questions for the Record from Mr. Gallo

SUBMITTED TO AGENCY FOR INTERNATIONAL DEVELOPMENT

MIXED CREDITS

Question. What role does A.I.D. play in combating the use of mixed credits by our competitors in their A.I.D. programs?

Answer. As part of the new Administration approach to mixed credits, A.I.D.—together with other agencies including the Eximbank—will take a more pro-active approach toward using mixed credits to advance our negotiations at the Organization for Economic Cooperation and Development (OECD). The goal of our negotiations is to eliminate mixed credits and our new strategy acknowledges that our negotiating leverage will be increased if the U.S. uses mixed credits to inflict costs to our competitors. An example of this new strategy is A.I.D.'s support for the AT&T bid, where we initiated a mixed credit rather than waiting to see what our competitors bid and then matching it.

TELECOMMUNICATIONS PROJECTS

Question. In the more advanced developing countries, there is a great need for telecommunications projects.

I am concerned that A.I.D. is not giving telecommunications projects enough attention.

Where do you see this as a priority?

Answer. A.I.D. does see telecommunications development as a high priority. A.I.D. has already obligated $345 million to support telecommunications projects in Egypt. Recently we supported AT&T's bid for a telecommunications project in Indonesia.

A relatively unknown fact of A.I.D.'s interest in telecommunications in Indonesia is that we have funded an American advisor to Minister Habibe who plays a key role in charting Indonesia's telecommunications development strategy. More advisors like these in key positions throughout the world could have substantial influence over telecommunications development projects.

SUBMITTED TO EXPORT-IMPORT BANK

LOAN DEMAND

Question. What is your current demand for direct credits? The War Chest? Medium-term loans? How much of this year's demand will be carried into next year?

Is expected demand from Eastern Europe included in these figures?

Answer. Eximbanker's loan authorizations through March 31, 1990 are $232.7 million. The Bank has $240 million in large loan offers outstanding that have a very high likelihood of being authorized this year. Further, the Bank expects about $165 million in medium-term loan demand for the balance of the year. Finally, the Bank expects to fully utilize the 1990 $110 million War Chest, either in 1990 or through offers made this year spilling over into 1991. We expect that the Bnak's 1990 loan demand will exceed authority by at least $100 million.

Not included in these projections is possible loan demand arising out of the emerging markets in Eastern Europe. This could be a significant factor in 1991, and could have some impact on 1990. We presently have several large Hungarian cases in house with a total of $152 million. It is not clear whether direct financing will be needed in any of these cases or whether they will convert this year or next.

EASTERN EUROPE MARKETS

Question. Is the FY91 Budget request for Exim sufficient to respond to additional demands from Eastern Europe?

In regard to FY91, given the cases in house from Hungary plus additional cases that might come from Poland or Yugoslavia (as well as Romania, East Germany, and Bulgaria, if and when we open for business in those countries) our annual demand for direct credits from Eastern Europe could reach the $200 million annual level.

In our view a large part of Eastern European capital requirements will be met through development aid on concessional terms, from both bilateral and multilateral sources. Projects that merit and can utilize conventional financing terms would benefit from Eximbank guarantees, which cover the political and commercial risk, and which facilitate access to medium and long-term financing, at marekt rates of interest, which can be fixed rates. Eximbank in FY'90 has ample guarantee authority to cover any expected increases in demand from Eastern Europe.

Some demand in Eastern Europe is likely to be for goods sold on short terms of 180 to 360 days, i.e., conventional trade financing, for which Eximbank has adequate insurance authority. This demand would be for items such as consumable and nondurable goods, raw materials, commodities, and semimanufactured components.

In January, an Eximbank team visited Poland and concluded that the short-term, private sector only TCIP program for Poland is not well suited to the needs of that country. Our team found that Poland needs medium and long-term financing much more than it needs short-term financing and that privatizing the public sector will be a long and difficult undertaking. In this connection, the Bank is now reviewing with AID and others in the government the possibility of offering medium-term credit.

Question. How to do we compete with other donor countries for market share in Eastern Europe?

Answer. Exim will compete utilizing all current authorities, including those made available under SEED I. It should be kept in mind that the Bank is demand driven. Consequently, we can only do business that is brought to us and won by U.S. suppliers. In addition, we can only approve those transactions that meet our legislative requirement for reasonable assurance of repayment.

Question. What is your estimate of Japan's use of their Export-Import Bank in Eastern Europe?

Answer. The most recent Berne Union report shows Japanese export credit support to be $20 million in Yugoslavia, $385 million in other Eastern European countries, and $3.2 billion in the Soviet Union, for a total of $3.6 billion.

Question. What are we up against? Who are the leaders and what is the amount of export credit available to Eastern Europe from our major trading partners?

Answer. The U.S. is up against some $30.7 billion in commitments from Western countries in export credit support to Yugoslavia, other Eastern European countries, and the Soviet Union. Austria has commitments of over $8 billion, Italy has $5.6 billion, and Germany is next with $5.4 billion. Japan's $3.6 billion is closely followed by France with $3.3 billion. Much of this, of course, represents outstanding balances on transactions and projects that have been undertaken over a period of decades. These are all higher than Eximbank's $1.9 billion. Our major Western European partners and Japan have an additional $6.5 billion in offers out to these countries.

Question. The Export-Import Bank held a conference in Washington last week that was very well attended. Can you give me a sense of where American businesses are with regard to these markets?

Answer. American businesses are at a very early stage of assessing the potential in these markets. They, however, are anxious to be competitive, and in this connection they are concerned about the role the Bank will play and the funds that will be available to support their export efforts. It appears, at this point, that most of the interest expressed by U.S. major exporters has been in the area of telecommunications, air traffic control systems, and agricultural food processing and other light industries in the emerging market economies of Eastern Europe and Central America.

Question. What kind of assistance are they looking for and what is the level of interest and commitment?

Answer. If attendance at the Conference's workshop on Eastern Europe is any indication, there appears to be a high level of interest in exporting to these markets. There does seem to be concern about the availability of the Bank to respond fully and adequately to all competitive situations in Eastern Europe. However, the actual extent of the commitment to these markets by U.S. exporters will be seen in time.

EXIMBANK APPROPRIATIONS

Question. Appropriations for the Eximbank have decreased over 90% in the last ten years. Yet Exim is one of the leading tools for U.S. development efforts. How can we change this in FY91?

Answer. The decline in Eximbank loan authority does pose a significant constraint to the Bank's availability to offer competitive financing, and may become a greater impediment if there is a surge in demand for U.S. exports; it does not, however, completely undermine the Bank's role as a policy instrument for U.S. development efforts. Through its insurance and guarantee programs, Eximbank can still serve as a powerful force for "bridging the gap" between the availability of private financing and the demands from LDC's, with their attendant credit, term, and interest rate risks.

Furthermore, recently the Bank and A.I.D. in a new cooperative effort on mixed credit transactions have worked together on certain developmental projects in East Asia, Africa and Latin America.

Similarly, whether by offering loans or guarantees, the Bank's receptivity to "risk" can serve as a catalyst in several ways. One is as a demonstration of support for economic restructuring and free market-based reform. Another is as a trailblazer, by setting a model for other export credit agencies, as well as private lenders, to follow. Often, other agencies wait for Eximbank to take the lead in a market, and then follow along. Furthermore, the IMF and IBRD often query Eximbank on its attitude, to help them establish a benchmark for their projections of likely bilateral credit flows.

TCIP AND EXPORT PROGRAMS FOR POLAND

Question. Have A.I.D. and Exim implemented the Trade Credit Insurance Program (TCIP) for Poland as mandated?

Answer. Eximbank and A.I.D. have concluded negotiations on the agreement setting forth the terms and conditions under which the TCIP will be operated. Signing of that agreement is expected shortly. Eximbank and AID have also held joint discussions with appropriate Polish entities to determine operating and securitizing arrangements. It is expected that the TCIP will be operational in the near future. In the meantime, Eximbank is open short-term as of March 1 for both the private and public sectors in Poland, on the understanding that AID will be reinsuring the Bank for private sector risk under the TCIP.

Question. What is the Eximbank doing to support U.S. exports to Poland?

Answer. On March 1, 1990, the Bank opened its short-term insurance program to Poland in advance of the implementation of the TCIP. Under this program, coverage will be available to either private or public sector buyers. This insurance protection protects the U.S. exporter against the risk of nonpayment by the foreign buyers and is offered through our agent, the Foreign Credit Insurance Association. The Bank's insurance program complements the $200 million TCIP program to private sector buyers. In addition, the Bank is presently reviewing with AID the possibility of offering medium-term credit to Poland.

INTEREST SUBSIDY PROGRAM

Question. What has happened to the interest subsidy program that we provided $20 million for in last year's bill?

Answer. The President's Cabinet-level Economic Policy Council reviewed the interest subsidy program in the context of the President's proposed FY'91 Budget and concluded that the Administration would not provide the requested authority for the program in FY'91. Following that decision regarding FY'91 it was determined that the same decision would also be applied to FY'90. The Council objected to this program on the grounds that it would be more expensive to operate than the direct credit program. It was viewed as a budget gimmick—a way of avoiding the budgetary costs of a direct loan program.

MEDIUM-TERM CREDIT CEILING

Question. How has the ceiling on the medium-term loans affected your ability to serve small business?

Answer. Pursuant to Public Law 101-167 (Foreign Operations, Export Financing, and Related Programs Appropriations Act, 1990, H.R. 3743), a limit of $215 million was established for the first time on the principal amount of the Bank's medium-term loan program, which is a subset of our direct lending ceiling. If the ceiling on medium-term loans remains in effect, it is projected that the Bank would exhaust its effect, it is projected that the Bank would exhaust its medium-term loan authority by the fourth quarter of FY 1990.

The medium-term loan program, which is very important in serving the needs of small and medium-size exporters, shows a fairly steady flow of activity, and is needed in order for U.S. firms to compete in a number of important markets.

Furthermore, in addition to the increasing demand for small and medium-sized exporters on our resources, we are beginning to process requests from the newly emerging markets of Eastern Europe and Central America. To meet the demands of these newly emerging markets, we will need to have greater flexibility in allocating our direct credit resources than the medium-term sub-limit presently allows.

A.I.D.'S MICRO-ENTERPRISE REPORT

Mr. **Obey**. At this point we will include in the record the Agency for International Development's report on the Micro-Enterprise Development Program requested in the fiscal year 1990 report.

[A.I.D.'s Micro-Enterprise Report follows:]

AGENCY FOR INTERNATIONAL DEVELOPMENT
WASHINGTON D C 20523

March 31, 1990

THE ADMINISTRATOR

The Honorable David R. Obey
Chairman
Subcommittee on Foreign Operations
Committee on Appropriations
House of Representatives
Washington, D.C. 20515

Dear Mr. Chairman:

I am pleased to submit the enclosed report to you on the Agency for International Development's (A.I.D.) microenterprise development program, as requested by the Conference Report accompanying the Foreign Assistance Appropriations Act for 1990.

I believe that broad-based economic growth is the most important means of assuring that poverty is sustainably reduced in developing countries. One of the most effective ways of involving the poor directly in this process is through microenterprise development. Recognizing this imperative since the mid-1970s, A.I.D. is proud to be among the leaders in supporting microenterprise survival through providing assistance and in searching for new means of helping these entrepreneurs and enterprises to succeed.

The enclosed report underscores the deep commitment A.I.D. has to achieving the above objectives. In addition to reviewing the diverse composition of A.I.D.'s microenterprise program, the report confirms that A.I.D. successfully met its FY 1988 and FY 1989 earmarked levels of $50 million and $75 million, respectively. Moreover, based on a recent canvas of A.I.D. field missions, I expect that the Agency will meet the $75 million earmarked for FY 1990. In light of absorptive capacity limitations in developing countries and in terms of competing budgetary needs within the Agency as a whole, the current level of effort and program mix, established during the last few years, should continue.

I would also note that, as the report points out, A.I.D. recently reorganized its microenterprise management and coordination office in Washington in order to assure continued excellence in this program. I share this commitment and wish to reassure you of my strong personal support for this program and for A.I.D.'s worldwide staff and cooperators who are carrying it out.

Please let me know if I can provide you with additional information on A.I.D.'s microenterprise development activities.

Sincerely,

Ronald W. Roskens

Enclosure: a/s

A.I.D. MICROENTERPRISE DEVELOPMENT PROGRAM

REPORT TO THE CONGRESS

U. S. Agency for International Development

March 30, 1990

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Acknowledgements: This report was prepared in the Employment and Enterprise Development Division of the Office of Rural and Institutional Development, Bureau for Science and Technology, of A.I.D., under the supervision of Michael Farbman and Ross Bigelow. The lead author was Elisabeth Rhyne. Assistance in data analysis was provided by Jennifer Santer and John Magill, Development Alternatives, Inc.

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EXECUTIVE SUMMARY

Poor people throughout the developing world create jobs and income for themselves, through microenterprises. A.I.D. has long been committed to microenterprise development, and now, thanks to interest from Congress and payoff from A.I.D.'s long term investment, A.I.D.'s support to microenterprise development is growing larger and more purposeful each year. This report, prepared to fulfill a Congressional request, presents the current status of those activities.[1]

In 1988 A.I.D.'s new funding for microenterprise development totaled $58.8 million; in 1989 it grew to $81.1 million; and in 1990 it is expected to reach $83.3 million. This support is widely distributed. Missions in 47 countries reported 170 separate projects with microenterprise activities, whose lifetime funding will total $390 million. About one-third of this support taps local currencies while two-thirds represents dollar obligations.

Beneficiary Characteristics

A.I.D. directs its microenterprise support toward the very smallest enterprises. At least half the projects work mainly with one and two person enterprises. Four-fifths of the projects work mainly with firms that employ five or fewer people. The microentrepreneurs A.I.D. assists are poor, but generally not the very poorest people. In the typical project, almost all of the microentrepreneurs (over 90 percent) are in the poorest half of the population, while a third are in the poorest 20 percent. It is likely that in many countries people engaging in a non-farm enterprise are almost by definition better off than the very poorest segments of society, so that A.I.D.'s beneficiary groups may well be a reflection of the underlying population of entrepreneurs.

The same may be true with respect to the participation of women. In the average A.I.D. project, 37 percent of microentrepreneurs are women. This figure may be less than 50 percent as a result of the proportion of entrepreneurs in a society who are women, but it may also reflect bias in assistance techniques that some projects employ. This is an area A.I.D. is targeting for further scrutiny and improvement.

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[1] This report draws on a February 1990 survey of all A.I.D. missions plus private voluntary and cooperative development organizations (PVOs and CDOs) supported by the Office of Private and Voluntary Cooperation in the Bureau of Food for Peace and Voluntary Assistance (FVA/PVC). Responsibility for determining which activities to include in these figures rests with missions, PVOs and CDOs who were charged to follow Policy Determination 17, "Microenterprise Development Program Guidelines."

A.I.D.'s Approach to Microenterprise Development

A.I.D. sees microenterprise development activities as a way to assist the poor to improve their lives through their own entrepreneurial activities. A.I.D. takes a business-oriented approach to microenterprise development. This business orientation in no way compromises commitment to the poor. Rather, the approach recognizes that even the smallest income-generating activities must master the same business realities as larger firms.

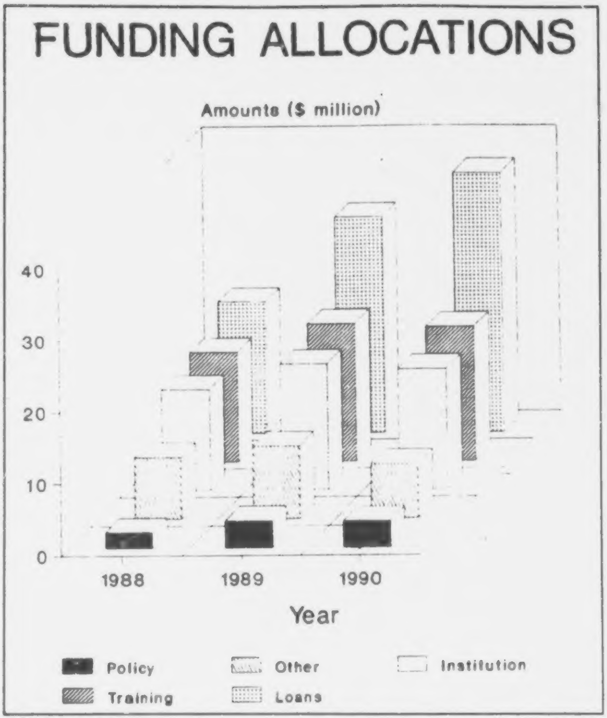

Figure 1

Every entrepreneur must satisfy four basic business needs: first, markets for their goods and services; second, access to resources; third, business and technical know-how; and fourth, a supportive environment. These four needs correspond to several key segments of A.I.D.'s microenterprise portfolio (See Figure 1). Access to resources is the focus of the credit activities which make up 44 percent of all microenterprise funding in 1990. Business and technical know-how are addressed through training and technical assistance activities, which absorb 23 percent of the portfolio. Roughly 4 percent of the portfolio supports policy and regulatory reform activities that help improve the environment for microenterprises. A.I.D. provides a great deal of additional support for policy reform and for sparking market growth, in the context of broader economic and sector policy programs. Through small farmer credit programs, for example, A.I.D. provides hundreds of millions of dollars of loans to the primary customers of microenterprise products and services. This is a significant market stimulus. Finally, through finance, technical assistance and training, A.I.D. supports the development of institutions capable of providing assistance to microenterprises. This is particularly important, as such capability was very limited only a few years ago. Institutional development accounts for 20 percent of A.I.D.'s total microenterprise funding.

Microenterprise Credit

Loans to microenterprises are the fastest growing part of A.I.D.'s microenterprise portfolio. The 1990 estimate of total lending is nearly double the 1988 level. This rapid growth reflects both an increased commitment on A.I.D.'s part, and increased capacity on the part of the specialized lending institutions that serve microenterprises.

A.I.D. believes that there is little sense in supporting lenders that cannot be self-sustaining in the long run. Therefore, in designing and supporting microenterprise credit projects it places highest priority on the prospects for financial self-sufficiency of the lending institution. Particular program terms, such as loan size, are determined in light of the needs of both beneficiaries and the lending institutions, rather than on the basis of an external, or a priori set of rules. Nevertheless, most of the microenterprise programs A.I.D. supports make very small loans. The average loan size for all microenterprise loans made with A.I.D. funding was $261 in 1988 and $313 in 1989.

A.I.D. has observed that most of the large, relatively successful credit programs, such as Grameen Bank in Bangladesh, Badan Kredit Kecamatan (BKK) in Indonesia, and the ACCION International programs in Latin America use a lending methodology that is sometimes called "minimalist'. This is a methodology which adapts its procedures for serving borrowers from the informal financial systems that are indigenous to many countries, but uses modern management techniques to track funds and reduce costs. It involves short term lending, with very little accompanying technical assistance, and reliance on the promise of repeat loans and personal character references to secure repayment, rather than collateral. A.I.D. plans to help equip an increasing number of programs to use minimalist principles in the coming years.

A.I.D.'s New Microenterprise Program

A.I.D.'s long involvement in microenterprise development is now maturing. We are reaching the point at which the agency's varied array of activities can be incorporated into a more cohesive microenterprise program. A.I.D. is already taking steps to bring this about. Budget constraints will not allow A.I.D. to expand significantly the amount of resources going into microenterprise by much, but consolidation of the activities into a more targeted and systematic program will mean that those resources have greater effect.

As part of the new program, A.I.D. has made plans to promote greater emphasis on three types of programs which have shown the potential to have a significant impact on microenterprises:

1) credit programs that use minimalist principles;

2) experimental forms of non-financial assistance; and

3) regulatory reform activities.

In addition, A.I.D. will continue to assist other organizations to enhance their capacity to carry out microenterprise programs, notably U.S.-based PVOs and their affiliates, and the Peace Corps.

The new emphasis will require an agency-wide effort of promotion and education, which will be carried out through the following steps:

- o Creation of a new Office of Small and Microenterprise Development within the Bureau for Private Enterprise to lead and coordinate A.I.D.'s efforts.
- o Encouragement of regional bureaus to increase their attention to microenterprise, including, if needed, the assignment of a full time microenterprise advisor, as the Africa Bureau has already done.
- o Launching of activities under the GEMINI (Growth and Equity through Microenterprise Investments and Institutions) Project, established in 1989 as a major resource for implementing new activities.
- o Creation, later this year, of the IRIS (Institutional Reform and the Informal Sector) Project, to focus on regulatory reform issues, and further support to the Institute for Liberty and Democracy in Peru to extend its experience to other countries.
- o Development of a monitoring system to better track both funding levels and achievements.
- o Conferences, workshops and cross-visits to noteworthy projects for A.I.D. staff and practitioners to accelerate learning.

PART I. A.I.D.'S APPROACH TO MICROENTERPRISE DEVELOPMENT

Throughout the developing world, the streets and marketplaces of both small villages and great cities are filled with vegetable stands, tea shops, bicycle repair shops, tailors, furniture makers, handicraft artisans, bakeries, and many other enterprises owned and operated by the poor. Recognizing that microenterprises are so important to the lives of the poor, and indeed, to developing economies as a whole, A.I.D. began to investigate ways to assist and promote them during the mid-1970s. In fact, A.I.D. has been at the forefront among both U.S. organizations and other donors in this effort. That commitment has paid off. Workable means of assistance have been developed, and the result is reflected in A.I.D.'s growing portfolio of successful microenterprise projects.

A. The Purpose of this Report

This report describes the current status of A.I.D.'s microenterprise development activities. It has been prepared at the request of the Congress, as stated in the Conference Report on the fiscal year 1990 Foreign Operations Appropriations Act. That report requested A.I.D. to submit:

> a detailed evaluation of the Micro-Enterprise Program. This evaluation should review the success of the program to date, the ability of A.I.D. to provide and monitor loans of less than $300 in poor countries and make recommendations on the size and scale of any future Micro-Enterprise Program.[2]

The report which follows has four parts. In this part the approach A.I.D. takes to microenterprise assistance is discussed, starting with a look at the needs of microenterprises. This part also reviews past A.I.D. contributions, the microenterprise legislation, and A.I.D.'s response to it.

In responding to the Congressional request, A.I.D. sent a questionnaire to all its missions, and its principal private voluntary organization (PVO) and cooperative development organization (CDO) grantees, seeking information on the amount of microenterprise funding for 1988, 1989 and 1990, types of programs supported by that funding, loan sizes, and beneficiary characteristics. With the help of the GEMINI project the responses have been examined, and inconsistencies in the data have been investigated and resolved. The resulting data have been tabulated, as presented in Part II of this report.

Part III states A.I.D.'s new plans for making its future microenterprise program more effective. A.I.D. recognizes that there is a continuing need to track the performance of its worldwide microenterprise activities and to provide decision-makers with regular information about its size and nature. Accordingly, A.I.D. has commissioned a study to lead to the creation of a monitoring and information system. The study is still in preparation, but preliminary considerations and findings are discussed in Part IV.

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[2] U.S. House of Representatives, Report 101-344, November 11, 1989, p. 18.

B. Who Are Microenterprises and Microentrepreneurs?

The definition one chooses for microenterprises will determine one's view of the problems the microenterprise development program should address. Unfortunately, a precise definition is notoriously difficult to pin down. The best definitions are qualitative. For example, microenterprises can be defined as the entrepreneurial activities of the poor. A frequently used alternate definition refers to those enterprises lacking access to conventional sources of capital, land, fixed premises, and business services. These definitions reflect the spirit of the term microenterprise. However, for purposes of program accountability, A.I.D. has adopted a more quantifiable definition, which is stated in its "Microenterprise Development Program Guidelines." This definition states that "a microenterprise should have no more than approximately 10 employees."[3] The guidelines note, however, that final judgment in specific instances should refer to the underlying concept, namely ownership of the enterprise by the poor. Larger community-based or cooperative enterprises are specifically included, when their members are poor.

Most of the enterprises that benefit from A.I.D.'s microenterprise support fall in the low end of the one-to-ten employee range. According to A.I.D.-sponsored research, self-employed people comprise by far the most numerous type of microenterprise, and in most countries more than 90 percent of microenterprises have fewer than 5 employees.[4] Although A.I.D.'s definition is broad, its program tends to focus at the small end of the size spectrum, simply because that is where most microenterprises are.

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[3] Policy Determination No. 17 (PD-17), October 10, 1988, p. 2.

[4] Carl Liedholm and Donald Mead, "Small Scale Industries in Developing Countries: Empirical Evidence and Policy Implications," MSU International Development Paper No. 9, Michigan State University, East Lansing, Michigan, 1987, p. 22.

C. Out of Poverty: The Goals of A.I.D.'s Microenterprise Program

A simple belief motivates A.I.D.'s involvement in microenterprise development. It is that for millions of the world's poorest people, the best hope for fighting poverty is to engage in their own entrepreneurial activities -- microenterprises. This is as true in the rural areas of Kenya where farmland is scarce and more than 29 percent of adults depend primarily on non-farm enterprises[5] as it is in the slums of Lima, Peru, where the possibilities of a job in the government or a formal sector business are impossibly far away for most of the poor. Throughout the developing world, poor people find that they must make their own opportunities.

If microenterprises represent one of the most important avenues the poor have for escaping poverty, international donors like A.I.D. should seek ways to help those enterprises succeed. Since recognizing this imperative in the late 1970s, A.I.D. has explored the needs of microentrepreneurs, seeking ways to support not just the survival, but also the growth of their enterprises.

A.I.D. has adopted a "business-oriented" approach to microenterprise development. This has been contrasted with a "poverty-alleviation" approach, but, while their methods may sometimes differ, in both cases the target population is the poorest of the economically active population and the smallest of enterprises. A.I.D.'s approach recognizes that there can be no poverty alleviation without the sustainable flow of income and employment from an on-going business. Regardless of the scale or level of an activity, it must exhibit some business-like characteristics in order to bring in income and create employment. Products or services offered must have a market and be competitively priced, so that the enterprise will survive and produce income, employment, and growth.

D. The Basic Needs of Microentrepreneurs

What does a business orientation to microenterprise development mean? For the smallest enterprises, as for the largest, there are four basic business needs: a market for their products or services; business and technical know-how; access to resources; and a supportive environment in which to pursue their trade. A serious lack of any of these basic needs leads to business failure, and in the case of the poor, business failure may threaten the entrepreneur's ability to supply her family's daily living requirements.

A.I.D.'s approach to microenterprise development is built around these four basic business needs. A.I.D. has found that each must be tackled in a different way, and in any particular situation, the needs that are lacking will determine the appropriate interventions. Box 1 and the paragraphs that immediately follow it describe what microenterprises need in each of these four areas, and outline the ways A.I.D. has found to assist them. The discussion differentiates between the activities that are clearly within the scope of microenterprise development and related activities that may also have an important impact on microenterprises.

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[5] Peter Kilby and Carl Liedholm, "The Role of Nonfarm Activities in the Rural Economy," S&T/RD/EED, EEPA Discussion Paper No. 7, 1986, p. 3.

BOX 1. THE FOUR BASIC BUSINESS NEEDS OF MICROENTERPRISES AND THE MEANS TO ADDRESS THEM

Microenterprise Programs*	Related Assistance
ACCESS TO RESOURCES: FINANCE	
credit programs savings programs support to informal financial systems	financial market policy reform
BUSINESS AND TECHNICAL KNOW-HOW	
training and technical assistance in business skills subsector-based assistance	vocational training appropriate technology programs
A SUPPORTIVE ENVIRONMENT	
assistance to microenterprise advocacy associations removal of barriers to formality construction of marketplaces and incubators	reform of economic policy toward small and microenterprises infrastructure
MARKETS FOR THEIR PRODUCTS AND SERVICES	
non-traditional export assistance subcontracting programs subsector-based assistance	general or regional demand-increasing actions, e.g.: small farmer assistance macroeconomic and sector reform

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* Activities in this column are counted towards the earmark when they are specifically directed at microenterprises.

1. Access to Resources: Finance

Every entrepreneur needs to be able to acquire business inputs: raw materials, tools and equipment, working or selling space, and labor. In some corners of the development community, there is frequently the presumption that credit is the solution to all of these problems. It is assumed that every entrepreneur needs to borrow in order to prosper. While A.I.D. agrees that credit is an extremely valuable service that outside donors can provide, it shies away from an exclusive focus on credit for two reasons: first, extensive research confirms that the overwhelming majority of poor entrepreneurs get the money to finance their businesses from their own savings, from family and friends or from informal financial systems.[6] Profits from farming or other enterprises, carefully saved, are often used to buy equipment for starting a microenterprise, and vice versa. Even in the United States, a country where access to credit for small business is a less severe constraint, only a fraction of small enterprises borrow. Most use savings and reinvested profits to buy what they need.

Second, A.I.D. cautions against an exclusive focus on credit because finance plays a supporting, rather than a leading role in any economy. Markets, skills and a supportive environment determine the potential for success of a business. Credit is powerless if these conditions are wanting.

That said, it is also true that in generally favorable circumstances, credit can be critical. Credit can be especially important for helping entrepreneurs to grow. A perhaps once-in-a-lifetime chance comes to a tailor in Malawi, for example, when he gets an order to make school uniforms for a local primary school. But without a short-term loan he may not be able to purchase the cloth to make them. If he gets the loan and fills the order, he may be able to market his services to other schools. If not, he will continue picking up orders one at a time from his ordinary customers. In short, credit can be very powerful.

A.I.D. has channeled most of its credit support through the non-governmental organizations that are often the only source of credit for poor potential borrowers other than informal lenders. In fact, it has been instrumental in supporting the development and dissemination of the minimalist loan-making methodology that underlies much of the current interest in poverty lending. A.I.D.'s role in developing this methodology will be discussed below, in section I.E.1.

2. Business and technical know-how

Given the highly competitive conditions that most microentrepreneurs face, they must be competent both in the technical aspects of their businesses and in management. Most microentrepreneurs develop these skills through informal systems of training. Parents pass down their business sense to their children, master craftsmen take on apprentices, and entrepreneurs learn simply through their own hard work and ingenuity. This tends to be sufficient for enterprises in markets that change slowly, and for enterprises that do not attempt to grow. However, as A.I.D.'s "Microenterprise Stocktaking Synthesis Report" points out, enterprises that are in the midst of growth or transition frequently need new levels of knowledge.[7] These entrepreneurs can benefit from outside assistance. This is true both for the very poorest who are attempting to operate an enterprise for the first time, moving out of absolute poverty, and for the microentrepreneur who is poised to expand her business from one employing two family members, to one with six or seven regular employees.

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[6] Liedholm and Mead, p. 39.

Business and technical skills can be transmitted in many ways, ranging from formal classroom training to indirect technical assistance. A.I.D. and U.S. private voluntary organizations have traditionally focused on training in business management, but A.I.D. is now exploring methodologies that help microenterprises deal with some of the more technical issues that are unique to particular product or service lines (subsector-based assistance). Whatever the nature of the assistance, strong local institutions, both formal and informal, are needed to deliver it.

3. A Supportive Environment

In countries throughout the developing world, governments have erected barriers to entry into the formal business world, by setting out requirements that the poorest people cannot meet. In Peru, an extreme example of this pathology, Hernando de Soto has documented both the costly requirements of complying with government regulations and the fact that the most dynamic part of the Peruvian economy operates "informally", that is, outside those regulations. However, the costs of being informal are high. They range from harassment by local authorities, to the lack of secure title to property, to the fact that informal enterprises cannot count on the legal validity of agreements or contracts they make. Throughout the world A.I.D. is supporting analyses of the relationships between the formal authorities and poor entrepreneurs, as well as joint action by groups of the poor themselves to seek change from governments.

National economic policy creates another set of conditions that microenterprises must face. These policies often determine the prices and availability of materials, energy and the like, as well as sales prices of goods and services produced. In many countries, these policies have been biased against small-scale and microenterprises. A.I.D. encourages governments to remove these biases. For example, when a country adopts market exchange rates and dismantles protection for import substitution industries, as A.I.D. often advocates, it makes it easier for the smallest enterprises to obtain imported tools, equipment or raw materials, inputs that otherwise would be available primarily to large firms. A wide array of policies A.I.D. promotes in its policy dialogue with developing countries work in similar ways.

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[7] James J. Boomgard, "A.I.D. Microenterprise Stocktaking: Synthesis Report," A.I.D. Evaluation Special Study No. 65, December 1989. pp. 12-13.

Basic infrastructure is another aspect of the general environment that should not be underestimated. Some students of development have argued that infrastructure has proven to be the single best determinant of improvement in the incomes of the poor, because infrastructure enables businesses to operate more efficiently and productively. Rural electrification allows entrepreneurs to switch from hand-operated to electric machines, which produces immediate results in the amount of time required to make products and in product quality. Village water supplies free women to work in microenterprises rather than spending time fetching water. Roads to poor areas provide access to markets that were previously unreachable.

4. A Market for Their Products or Services

Having a market for the goods and services produced is probably the most important of the four needs, though it is often difficult to satisfy. Most microentrepreneurs sell their products to poor consumers, (though there are also important markets for some enterprises among middle class consumers, larger businesses, local governments, and even exporters). Therefore, probably the best way to promote microenterprises is to make sure that the poor have increasing purchasing power. In developing countries that are dominated by agriculture (the majority of them), most poor consumers are small farmers. This means that a healthy, growing agricultural sector is an important, if not the important, precondition for microenterprise growth. By devoting a very substantial share of its total budget to small farm agriculture, A.I.D. has long been supporting microenterprises in a crucially important, though indirect, way. [8]

While the poor remain the main outlet for microenterprise services and products, some other markets offer more growth potential, such as the provision of inputs to medium and large-scale businesses and exporters. When they connect with these markets, microentrepreneurs reach beyond the limited resources of poor communities, to buyers with far more money. Handicraft producers who sell to exporters can tap into the purses of affluent first world consumers. In the process, they bring additional sources of money into their own communities, rather than merely recirculating the meager resources already available. Reaching such markets is not easy for microentrepreneurs. They need to know how to find potential buyers, what kinds of products are in demand, how to meet quality standards, and the like. Because of their social position, it is often quite difficult for poor, uneducated people to get such information, especially working alone. A.I.D. sponsors programs that help microentrepreneurs to organize themselves so that they can negotiate with larger buyers, funds industry specialists to act as brokers between microentrepreneurs and larger buyers, and supports a wide variety of other approaches that pave the way for microenterprises to break out of limited markets. And when such highly leveraged interventions are successful, they may benefit a whole group, class, or industry subsector of producers, not just a few individuals.

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[8] Small farmer assistance is not counted in A.I.D.'s microenterprise program totals.

Microenterprises generally grow best if the economy as a whole is growing, and growth requires a sound macroeconomic environment. The economic policies A.I.D. advocates at the national level seek to create growth. In particular, they seek to promote a type of economic growth in which the poor can participate.

A.I.D. does not count its support to macroeconomic policy reform, infrastructure, or agriculture as part of microenterprise development. However, it is important to understand that these diverse indirect interventions can be as important to the development of microenterprises as any form of direct assistance.

In summary, A.I.D.'s microenterprise program is built around addressing these four basic business needs: markets, skills, resources, and a supportive environment. The next section of the report gives a brief history of how A.I.D. has developed this program during the recent past.

E. A.I.D.'s Contribution to Microenterprise Development

1. Early Initiatives

A.I.D.'s commitment to microenterprise development has grown steadily since the late 1970s.[9] At the beginning, governments, donors and private voluntary organizations were just beginning to examine the potential for working with small-scale and microenterprises, amidst significant skepticism that such work would be either successful or particularly important for economic development. A.I.D. sponsored investigations that have helped the development community at large to learn about microenterprises, and to develop proficiency in assisting them. A.I.D's work provided two very clear and important findings. These appear so obvious today that it is hard to remember that they were not widely believed just a decade ago.

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[9] A.I.D. has sponsored a number of centrally-funded projects to study the nature of microenterprises and ways to assist them, and to transfer this knowledge to A.I.D. missions and to operational projects in developing countries. Among these projects are: The Off-Farm Employment Project; the Small Enterprise Approaches to Employment Project, with components: 1) Program for Investment in the Small Capital Enterprise Sector (PISCES), 2) the small-scale enterprise project's evaluation component, 3) Michigan State University research components, and 4) Assistance to Resource Institutions for Enterprise Support (ARIES); the Small Business Capacity Development Project; CDIE Evaluations (Searching for Benefits, and Microenterprise Stocktaking, among others); the Employment and Enterprise Policy Analysis project; the Growth and Equity through Microenterprise Investments and Institutions (GEMINI) project, and (in preparation) the Institutional Reform and the Informal Sector (IRIS) project.

First, A.I.D.-sponsored research demonstrated that small and microenterprises make important contributions to economic and social well-being in poor societies. This research, carried out largely by Michigan State University (MSU), has been particularly important in proving to the leaders of governments and development organizations that even the very smallest microenterprises, of fewer than five members, were economically productive. The diffusion of these findings has increased the interest in microenterprise assistance. MSU's studies, carried out in more than ten countries, produced data that are probably the single largest source of information on the composition, characteristics and performance of small-scale and microenterprises. The data show clearly that in many countries small-scale and microenterprises produce as many jobs, and in some cases as great a share of GNP, as large enterprises. In most countries, small-scale and microenterprises are the top source of jobs other than agriculture. The research also showed that contrary to some conventional wisdom, the demand for the products of these enterprises is growing, and that small enterprises make profitable investments.

Second, A.I.D.-sponsored studies and pilot projects in developing countries confirmed that it is possible to provide assistance to small-scale and microenterprises effectively. These studies were done under the PISCES (Program for Investment in the Small Capital Enterprise Sector) project, carried out by ACCION International, the Development Group for Alternative Policies, and Partnership for Productivity, and through a series of evaluations carried out by Development Alternatives, Inc. (DAI). The widely read PISCES studies and DAI evaluations have played an important role in increasing worldwide interest in microenterprise development to its current level.

One aspect of that work of which A.I.D. is particularly proud is its part in demonstrating that poor microentrepreneurs are good credit risks and that programs serving them can cover operating costs. These findings ran against the conventional wisdom of many donors at the time. A.I.D. has helped refine and spread the lending methodology known as minimalist credit, which underlies much of today's interest in microenterprise lending. During its work on PISCES, the U.S. PVO ACCION had the opportunity to identify and test this methodology widely for the first time. ACCION's subsequent success in applying this methodology has led both to recognition of ACCION as a leader in microenterprise development, and to the methodology's growing acceptance throughout Latin America. DAI's evaluation of the Badan Kredit Kecamatan (BKK) program in Indonesia, a program that uses a similar methodology, has been and continues to be influential. It has introduced many people to the principles of minimalist lending and convinced them that the methodology offers the potential to be self-sustaining and to serve large numbers of borrowers.

Another important contribution of A.I.D.'s work in microenterprise development has been to build the managerial capacity of the local organizations and U.S. PVOs that implement microenterprise programs. PISCES concluded that microenterprise programs failed most often because the implementing organizations were not able to handle the management tasks required to run their programs in a businesslike way. Under the ARIES (Assistance to Resource Institutions for Enterprise Support) project, Nathan Associates and Harvard Institute for International Development have worked with such organizations directly and have developed training materials that help organizations improve their performance, particularly in the areas of strategic planning and financial management.

At the same time that it implemented these centrally-funded research projects, A.I.D. has been quietly supporting a growing portfolio of microenterprise projects throughout the world. In early 1989, an A.I.D. report provided information on 87 active microenterprise development projects, in 35 countries, with total life-of-project funding of $290 million.[10] In addition, the Office of Private and Voluntary Cooperation, in the Bureau for Food for Peace and Voluntary Assistance (FVA/PVC), has for several years been funding the microenterprise programs of U.S. private voluntary organizations and cooperative development organizations. For example, ACCION has received four matching grants since 1979 that have enabled it to extend its programs throughout Latin America. About 24 percent of FVA/PVC's funding for new matching grants awarded this year will go to PVO microenterprise programs.

2. The GEMINI (Growth and Equity through Microenterprise Investments and Institutions) Project

The GEMINI project is one of the major vehicles through which A.I.D. will strengthen its microenterprise program in the next five years. This project, begun in October 1989, was developed as a direct response to growing interest in microenterprise development in Congress and in the development community. It will work directly with missions in the design and execution of their microenterprise activities and will carry out research and development to further the state of knowledge about microenterprise assistance. The GEMINI project will bring academics, A.I.D., PVOs and other practitioners together to address questions in three important areas:

- How do microenterprises behave over time? Growth patterns will be examined, to help understand what factors and interventions contribute to a microenterprise's growth (or failure); how microenterprises contribute to overall economic development in a country; and to discover how often microenterprises "graduate" to become small and medium-sized firms.

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[10] William Doyle and Joseph Lieberson, "Microenterprise Stocktaking: A Statistical Look at A.I.D.'s Microenterprise Portfolio," A.I.D. Evaluation Special Study No. 63. A.I.D./PPC/CDIE, 1989. p. 2.

- Methods for assisting microenterprises. Most of GEMINI's work on credit methodologies will focus on enabling credit programs to expand and become integrated into local financial systems. GEMINI will also experiment with new methods of non-financial assistance, especially methods that respond to the competitive circumstances of entrepreneurs, such as subsector-based assistance.

- Developing the capacity of local institutions to carry out microenterprise programs. Picking up from ARIES, GEMINI will provide training, including regional workshops and training for host country microenterprise practitioners and A.I.D. staff.

The GEMINI team combines institutions that have contributed a great deal to the field of microenterprise development. The project is led by Development Alternatives, Inc., with Michigan State University, four specialized PVOs (ACCION, Technoserve, Opportunity International and World Education), and Management Systems International, a consulting firm.

3. Collaboration with the Peace Corps

Although Peace Corps volunteers have worked with small businesses in thousands of poor communities since the early 1960s, it was not until 1983 that it formally established a small business development program. Today, over 3,500 volunteers are involved in small and microenterprise development in some 60 countries.

In 1988, the late A.I.D. Administrator Alan Woods joined Peace Corps Director Loret Ruppe in signing a memorandum of understanding to launch a two-year Microenterprise Development Program (MEDP). The purpose of the program was to build on existing collaboration between the two agencies to:

- Develop a cadre of skilled microenterprise volunteers and counterparts who could train others in their communities; and

- Increase the ability of local microenterprise development institutions and persons to utilize A.I.D. or other donor resources -- both financial and non-financial -- for their own development.

Under a Participating Agency Service Agreement (PASA), A.I.D. obligated $1.1 million to the Peace Corps for MEDP activities in 1988 and 1989. Programs have been launched in Botswana, Mali, Ghana, Kenya, Costa Rica, Honduras, the Dominican Republic, Guatemala, Fiji, and Western Samoa. Technical training in enterprise development, the development of training materials, and the sharing of experience and information through international workshops have taken place using A.I.D. resources.

In March 1990, some 70 Peace Corps, A.I.D. and host-country leaders gathered for the first time to review lessons learned from the two years of work in MEDP and to make recommendations for the future. With fifteen participating countries represented, conferees drew on a wide array of practical experiences, clarified MEDP objectives, examined specific country programs, and assessed technical needs and resources available for addressing them. Conference participants reaffirmed their commitment to joint work on microenterprise development, and proposed that the collaboration under MEDP be extended through at least 1992. A report on the proceedings of the conference will be issued shortly.

F. The Microenterprise Legislation, and A.I.D.'s Response

In the Continuing Resolution for fiscal year 1988, the Congress included language requiring that A.I.D. devote at least $50 million of that year's dollar obligations or local currency expenditures to "programs of credit and other assistance for micro-enterprises."[11] This legislation, and the discussions surrounding its passage, coincided with an increased interest in microenterprise coming from within A.I.D. The result has been increased attention to and action on microenterprise development during 1988 and 1989, which continues today. A.I.D. has responded to the legislation as the following sections describe.

1. The Advisory Committee on Microenterprise

The Committee Report that accompanied the FY 1988 Continuing Resolution called on the A.I.D. Administrator to "appoint an advisory committee composed of individuals from nongovernmental organizations who have experience in implementation of micro-enterprise credit projects in developing countries to assist the Administrator in developing the guidelines for this program."[12] A.I.D. appointed a committee of 17 individuals, chosen by the Administrator for their expertise in the field of microenterprise. The principal task of this committee has been to provide advice on the guidelines A.I.D. uses to define its microenterprise program. The Committee reviewed, commented on, and finally approved the guidelines which A.I.D. drafted. These guidelines have since been issued as a formal A.I.D. policy determination, PD-17, "Microenterprise Development Program Guidelines." Subsequently, the Committee reviewed the microenterprise stocktaking reports that A.I.D. commissioned to gain a better understanding of the nature of its microenterprise portfolio. In its most recent meeting, on February 16, 1990, the Committee recommended some key changes in the guidelines, discussed below, and further recommended some specific actions A.I.D. should take to assure that its microenterprise program continues to focus strongly on credit for the poorest entrepreneurs.[13]

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[11] Continuing Resolution for Fiscal Year 1988, p. 144.

[12] Committee on Appropriations, U.S. House of Representatives. Report on FY 1988 Continuing Resolution. p. 816.

2. Guidelines

The guidelines enunciated in PD-17 play a central role in A.I.D.'s response to the microenterprise legislation. The guidelines, together with the annual budget process, are the formal vehicles through which A.I.D. implements the legislation. The guidelines determine what activities can be counted towards the microenterprise earmark, and the budget process directs funding into such activities.

The guidelines deal, among other things, with four issues that the Congress considered during the debate over the legislation: loan size, poverty level of beneficiaries, gender of beneficiaries, and types of activities that fit within the microenterprise program. Some proposed versions of the legislation had originally called for the program to cover loans only, with a maximum loan size of $300. Half of the loans were to go to women, and all the loans were to go to the poor, variously defined as the poorest 20 percent or the poorest 50 percent of the population. As the legislation was discussed with A.I.D. and other experts in the field, it was decided that a good microenterprise program would require greater flexibility than these parameters allowed. The statute, as finally passed, contained none of these restrictions. Report language accompanying the legislation "urged" and "recommended" that A.I.D. meet the target levels as often as possible.

The guidelines adopted by A.I.D. reflect some of this tension between the need for flexibility in programming and the desire to promote poverty lending. They state the following:

- o This earmark may be met through the funding of credit, technical assistance, training, or related activities directed at microenterprises.

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[13] The Advisory Committee's report has not yet been presented to A.I.D. Statements here about its most recent actions stem from votes taken in the Committee's public meeting in February 1990.

- The average loan size should not exceed $300 unless there are indications that larger-sized loans are needed to achieve the objectives of this program.

- Programs should be designed ideally to ... make at least 50 percent of their resources (credit, technical, and training) available to women-owned and -operated businesses.

- Missions should note that the conference report accompanying the appropriations legislation suggested some levels or classifications of program beneficiaries: (a) individuals in the poorest 50 percent of the populations, ... and (c) businesses owned and operated by the poorest 20 percent of the population.[14]

In short, A.I.D.'s guidelines reflect the spirit of the report language in directing the agency to emphasize small loans for the poor, while explicitly allowing the microenterprise program to be broader in scope than credit and more flexible in its terms, as the statutory language permits.

A.I.D. maintains that it met the earmark in fiscal years 1988 and 1989, by funding more than $50 million and $75 million, respectively, of new activities that fall within the guidelines offered by PD-17, using the full flexibility that they provide.
Part II of this report details funding levels.

3. The Stocktaking Exercise

During 1988 and 1989, A.I.D. undertook an extensive review of its past and present microenterprise portfolio. This thorough investigation sought to discover "what works best under what conditions."[15] The stocktaking exercise developed a data base of 32 selected projects, many of which were evaluated on-site. The purpose of this exercise was not to check on A.I.D.'s compliance with the earmark. In fact, the exercise sought to capture A.I.D.'s recent past experience. The reports examined the nature of the microenterprise activities receiving A.I.D. support, seeking to understand the issues that would be involved in creating a stronger microenterprise program in the agency.

The stocktaking report revealed that A.I.D.'s microenterprise portfolio was indeed a broadly conceived program oriented toward growth. It showed that A.I.D.'s support was fairly evenly divided between enterprise formation programs that help the poorest people start income-generating activities, enterprise expansion programs that help established microenterprises grow, and enterprise transformation programs that help turn the most successful microenterprises into more sophisticated small businesses.

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[14] The four bullets are from PD-17, pp. 2, 4, 3 and 3, respectively.

[15] Boomgard, p. vii.

The assistance methodologies applied were quite diverse, ranging from pure credit, to mixed credit and technical assistance, to pure technical assistance. Among the credit programs, average loan size ranged from $508 for the formation programs, to $705 for expansion programs, to $3,261 for transformation programs.[16] Women's participation was near or over 50 percent in the formation and expansion programs, but substantially lower in the transformation programs. Finally, it was found that while almost all microentrepreneurs were clearly poor, they were not the poorest of the poor, largely because the poorest were not involved in self-employment, but some other type of activity, such as subsistence agriculture. It also concluded that microenterprise programs had the greatest impact on the poor through increased employment in assisted microenterprises, and challenged the presumption of some "that the jobs created are inferior in income, risk, or working conditions to self-employment."[17]

4. Advisory Committee's Response to the Stocktaking

In its review of the stocktaking report, the Advisory Committee on Microenterprise affirmed the tenor of A.I.D.'s program with respect to its breadth of approach and its success in reaching women. However, it noted that there was a significant discrepancy between the size of A.I.D.'s loans and the target of $300. The Committee considered whether it was more appropriate to ask A.I.D. to change its program or to change the PD-17 guidance on loan size. It chose the latter course, after committee members commented that:

- In some countries, cost structures were such that $300 was too small even for loans to the very poor.
- A $300 limit would not allow for A.I.D.'s program to serve the full range of microenterprises that lacked access to credit, and thus implied a strong preference for self-employment over job creation through enterprise growth.
- Long run viability of lending institutions often demanded that loan sizes

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[16] Boomgard, p. 73.

[17] Boomgard, pp. 54-55.

> be mixed, in order to improve portfolio diversification and spread administrative costs.

The Committee acknowledged that in eliminating the $300 target, A.I.D. would lose a simple, though imperfect, criterion for ensuring that benefits would go to the very poor. In a unanimous decision, the Committee voted that the $300 loan recommendation be dropped from PD-17, and charged A.I.D. to develop other measures that would conclusively show that the activities indeed reached the poor.

PART II. THE STATUS OF A.I.D.'S MICROENTERPRISE ACTIVITIES

According to data collected from A.I.D. field missions and Washington offices in February 1990, A.I.D. provided $58.8 million of new funding for microenterprise development in 1988, $81.1 million in 1989, and expects to provide $83.3 million in 1990 (see Table 1).[18] This funding supports a multi-faceted set of activities. In 1990, 44 percent of the total will be used for loans to microenterprises; 23 percent for training and technical assistance to entrepreneurs; 20 percent for support to implementing institutions; 4 percent for policy and regulatory reform activities; and the remaining 9 percent for a mixture of several types of assistance (such as in-kind grants of tools and equipment, or building premises for microenterprises). A.I.D. is carrying out microenterprise activities in 47 countries. The total number of projects identified is 170, and these projects will, over their lifetimes, provide $390 million in assistance to microenterprises. Roughly two-thirds of A.I.D.'s microenterprise activities are funded from U.S. dollar obligations and one-third are from local currency generations.

TABLE 1. SUMMARY OF A.I.D'S MICROENTERPRISE ACTIVITIES
(in thousands of dollars)

ACTIVITY TYPE	1988 ACTUAL	1989 ACTUAL	1990 ESTIMATE	LIFE OF PROJECT
Loans to Enterprises	18,434	30,255	36,374	124,051
Training and Tech. Assistance	15,350	19,294	18,810	115,985
Institutional Development	14,165	17,666	16,876	89,081
Policy and Regulatory Reform	2,182	3,735	3,625	13,504
Other	8,700	10,149	7,631	47,489
TOTAL	58,831	81,099	83,316	390,110

The enterprises receiving assistance are indeed very small. For each separate project, missions reported on the average number of employees in the assisted enterprises. For 1988, the median project reported an average enterprise size of one. In 1989, that figure was two. In other words, half the projects are working mainly with one or two person enterprises. The remaining projects work with a mix of enterprise sizes, up through ten employees, but even these projects are oriented towards the smaller firms. Only 26 of the 132 projects reporting on size of enterprises showed the average number of employees to be above five.

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[18] These figures vary slightly from those reported previously for two reasons. First, A.I.D. missions are following the guidelines of PD-17 more closely in determining what to include as microenterprise activities. Second, these totals only cover mission-funded activities and support to PVOs and CDOs provided by FVA/PVC. Other centrally-funded activities are not included in the totals. Figures reported in this document should be considered as superseding estimates reported on earlier occasions.

A.I.D.'s support does reach the poor. In the median A.I.D.-supported project, 90 percent of the beneficiaries are in the poorest half of the population (see Figure 2).[19]

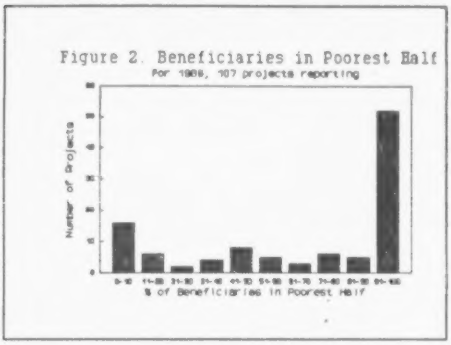

Figure 2. Beneficiaries in Poorest Half

For 1989, 107 projects reporting

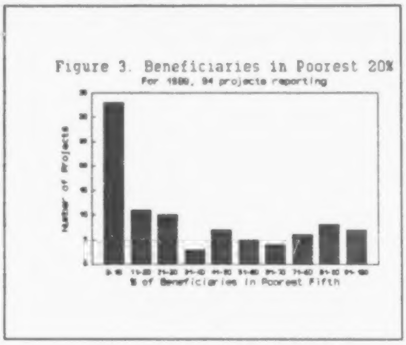

Figure 3. Beneficiaries in Poorest 20%

For 1989, 94 projects reporting

However, the majority of beneficiaries in most programs are not in the very poorest group, the lowest fifth of the income distribution. In the average program for 1989, 37 percent of beneficiaries are reported to be in the very poorest income group (see Figure 3).[20] In interpreting this information, it is important to note that in many countries, particularly in Africa, the overwhelming majority of the population is poor, so that a program would not have to reach the lowest group to reach the truly poor. Moreover, in many of these same countries, the very poorest group consists largely of people who do not engage in microenterprise activities, such as subsistence farmers, laborers, or dependents (children, the aged, the infirm), or people who live in remote areas where microenterprise projects do not operate. Put another way, the very fact that someone is carrying on an enterprise activity may place that person above a significant fraction of the rest of the population. A handful of the reported projects serve primarily beneficiaries above the 50 percent mark. A.I.D. will review these projects to determine why missions have counted them as microenterprise activities.[21]

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[19] Beneficiaries are defined as the microentrepreneurs who own the enterprises. Data on the income levels of their employees is not available. If it were, it would likely show an even greater impact on the poor.

[20] Data on beneficiary characteristics are not available for all programs. In general, A.I.D. field missions were able to report on the proportion of female beneficiaries, except where benefits to microenterprises were indirect, as in some institutional support and policy reform activities. Data on the poverty level of beneficiaries were less frequently available, at least in the form requested. For example, the Dominican Republic mission reported that it could obtain income data on beneficiaries; however, as no national income distribution survey has been done since 1984, it could not reliably translate income figures into population percentiles.

A.I.D.'s projects for the most part serve substantial numbers of female entrepreneurs, but there is room for improvement. In the average program for 1989, 37 percent of the beneficiaries were women. A few programs are directed almost entirely at women, but others serve mainly men (See Figure 4). A.I.D. will review the programs with very low female participation to identify and reduce obstacles to women's participation inherent in their design.

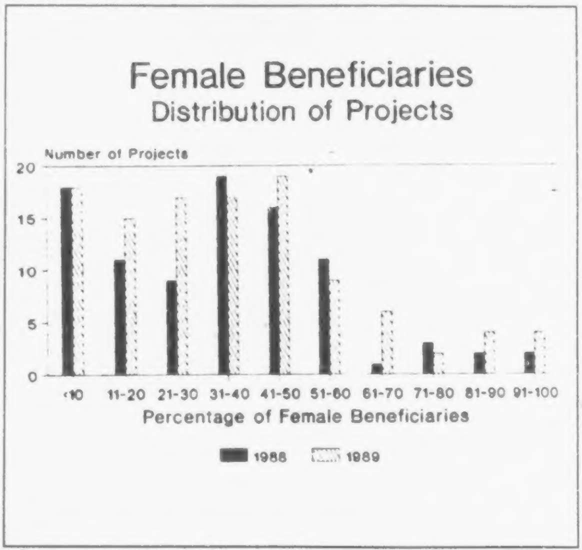

Figure 4

A.I.D.'s support to microenterprises is fairly evenly divided among the three geographic regions, with 5 percent of the 1989 total coming from centrally-funded support to PVOs and CDOs (see Figure 5). Africa received the largest share in 1989. Funding for microenterprise development is growing rapidly in Africa, while remaining relatively stable in the other two regions. The character of support to microenterprises shows clear regional patterns. Projects in Latin America are heavily oriented toward credit, with more than two thirds of all funding in 1989 and 1990 supporting loans (see Annex Table 2). In the other two regions, activities are more evenly split among all program types. In Africa the lower relative level of funding for credit may reflect a

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[21] Such reviews could not be completed as part of this data collection effort. This report relies on determinations made by missions in light of PD-17 guidance.

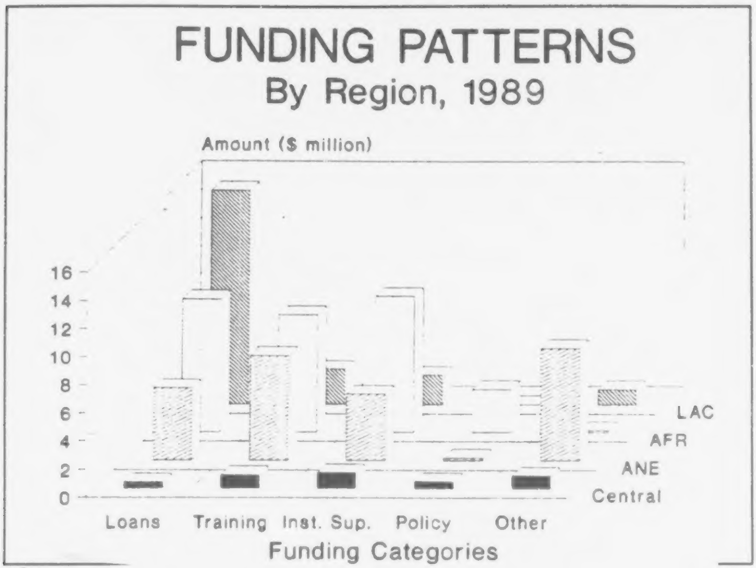

Figure 5

paucity of institutions capable of supporting large credit funds and the consequent greater investment in institutional development. In Asia, a large share of funds (31 percent in 1989) goes to other types of programs, such as direct grants, of money or tools and equipment, and construction of market premises.

To explore these data further, it is useful to examine how A.I.D.'s activities address each of the four basic business needs of microenterprises: access to resources through finance, technical and business know-how, a supportive environment, and markets. In addition, a closer look at A.I.D.'s institutional development activities is needed.

A. A.I.D.'s Approach to Credit

Microenterprise credit programs address the inability of the poor to get credit from formal financial institutions. This problem affects microentrepreneurs with business activities of all sizes. Commercial banks and most government development banks simply do not serve the genuinely poor. A.I.D. and others are beginning to share a vision of a time when this problem largely will be solved, through the operation of specialized financial institutions that have learned to lend to microenterprises at very low or no subsidy. That time is not yet here, but the accomplishments of programs like BKK, KUPEDES, Grameen Bank and ACCION International have given promise that the vision may eventually be realized. (See Box 2 for a discussion of ADEMI, an ACCION affiliate that epitomizes A.I.D.'s aspirations in microenterprise credit.) This vision depends on the birth, nurturing and growth of sound institutions whose purposes include the provision of credit and other services to poor microentrepreneurs. If we take such a perspective, it is immediately apparent that what matters most is helping institutions to reach large numbers of the poor, with low or no subsidy. Loan size and other particular terms of a program must be decided in view of the health of each institution, not in advance or from outside. The large, successful microenterprise lending institutions differ from each other in many respects, including size of loans, lending mechanics, use of group lending, and loan terms. What they have in common are lending methodologies that blend informal finance techniques with modern, streamlined credit management. This method is often called minimalist credit, and is illustrated in Box 2 by the ADEMI project. It involves short term loans, with very little accompanying technical assistance, and reliance on the prospect of repeat loan to motivate borrowers to repay.

A.I.D.'s microenterprise portfolio reflects the fact that the elements of success in this difficult endeavor are only beginning to be understood. There simply are not very many institutions throughout the developing world that have demonstrated the potential to become large, low-subsidy microenterprise lenders. A.I.D. cannot create an ADEMI simply by providing funds, because local talent and commitment are essential, but A.I.D. can assist institutions that show promise. However, until credit programs show that they are on the track that leads to expansion and sustainability, the amounts of funding that A.I.D. can justify are limited.

Given continued institutional development, however, A.I.D. has been able to increase the amount of funding it devotes to microenterprise lending rather rapidly. In 1989, A.I.D. supplied $30.3 million in funding for microenterprise lending, up from $18.4 million in 1988. It expects to supply $36.4 million in 1990. In other words, A.I.D.'s funding for credit has nearly doubled in two years. This credit portfolio is clearly micro. It is not directed primarily toward the upper end of the size distribution, but serves microenterprises of all sizes and types. The average loan size was $261 in 1988 and $313 in 1989 (see Table 2)[22]. Nearly half of all the loans A.I.D. finances for microenterprises are smaller than $300.

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[22] Figures in Table 2 are based on loans made (that is, expenditures by the lending organization), while those in Table 1 and the Annex Tables are based on A.I.D.'s dollar obligations and commitments of local currencies to the organizations. Therefore, they are not directly comparable.

BOX 2. ADEMI: CREDIT FOR MICROENTERPRISE GROWTH

A.I.D.'S philosophy toward microenterprise credit is well illustrated by the example of ADEMI (La Asociacion para el Desarrollo de Microempresas, Inc.) in the Dominican Republic. A group of prominent local citizens started ADEMI in 1983, with technical support from ACCION International and, shortly thereafter, financial support from A.I.D., to serve poor entrepreneurs. ADEMI set its sights on growth: both for its own operations and for the enterprises of its borrowers. It aimed to become a nationwide program that would make a difference in the incomes, jobs and well-being of the poor, and through this to contribute to the economic and democratic development of the Dominican Republic. As businessmen, the founders of ADEMI saw that the bottom line for the program was financial self-sufficiency. This would enable it to raise the large amounts of funds needed to reach throughout the nation, and to continue to serve those borrowers year after year. ADEMI's program is designed to achieve financial self-sufficiency.

- Its lending methodology is both low-cost and convenient for borrowers.
- Interest rates and fees cover the cost of funds and operations.
- Advanced information systems enable management to keep close tabs on performance.
- Borrowers are motivated to repay by the prospect of repeat loans.
- ADEMI seeks new clients while continuing to serve its growing older clients.

As a result of its businesslike approach, ADEMI has in six years expanded from one to 20 branch offices. It serves approximately 7,000 active clients, including about 300 new clients per month, a significant share of the total microenterprise population. Remarkably, its interest income now covers all of its operating costs and costs of borrowing, which includes interest on a sizeable private commercial bank loan.

ADEMI's growth orientation extends to its clients. It focuses on production enterprises, because of their growth potential. The job creation and multiplier effects of a growing enterprise bring income into the poorest areas. ADEMI estimates that one new job is created for every $1,000 lent. The following anecdote illustrates how ADEMI stays with its clients as they grow.

Seven years ago, Teofilo bought cups, plates, and vases and sold them on the streets. He barely made enough money to survive. Today, he is a small manufacturer of ceramics, with 40 employees, two workshops, and 10 imported kilns. He attributes much of his success to the support he received from ADEMI. Teofilo used his $150 first loan to purchase finished goods which he then sold. ADEMI continued to lend gradually larger amounts to him as his business grew, and as he showed that he could repay. He put aside enough money to invest in the equipment needed to manufacture the ceramics, again with the help of an ADEMI loan. Within a few years, Teofilo's business was thriving and he had hired several workers, but it was still far too small and lacking in collateral for commercial bank standards. At this point, Teofilo's credit needs had progressed well above $1,000. ADEMI's staff realized that he had nowhere to turn, except ADEMI itself. They have continued to finance Teofilo's business. Teofilo has also helped a large number of youngsters from his rural home town to get a good start. His workshop has become an on-the-job training program for tens of unskilled youth whose alternative is unemployment. Some will probably start their own enterprises, and become ADEMI clients.

TABLE 2. A.I.D'S MICROENTERPRISE LENDING (Summary Statistics)

	ALL LOANS		LOANS UNDER $300	
ACTIVITY TYPE	1988	1989	1988	1989
Number of loans	80,535	103,735	41,313	46,360
Amount ('000)	$21,320	$32,569	$5,540	$5,525
Average loan size	$261	$313	$134	$119

Some of the programs A.I.D. supports focus on a particular loan size, but many others lend across a range from less than $100 to more than $1,000. Within this range, a seamstress in Honduras can progress from buying pieces of cloth to sew on a rented sewing machine, to purchasing her own machine. An important lesson from microenterprise programs that include a range of loan sizes is that an orientation toward microenterprise growth is highly compatible with a commitment to the poor. The growth and employment creation that results from staying with enterprises as they grow may provide more income for the poor than a strategy that has an arbitrary cut-off point.

B. Business and Technical Skills: Non-Financial Assistance

Development professionals who work with microenterprises throughout the world recognize that microenterprises do not always need to borrow money, but instead often lack critical business or technical skills. This understanding is particularly important in determining the most appropriate intervention to help the poorest people just starting an income-generating activity (enterprise formation) and for microenterprises seeking to grow to a new level of sophistication (enterprise transformation). Because of their close connection to growth, training and technical assistance always have been an important part of A.I.D.'s assistance to microenterprises. A.I.D.'s support for training and technical assistance has been growing slowly from $15.4 million in 1988 to $18.8 million projected for 1990. These activities account for about a quarter of the whole microenterprise portfolio.

However, the area of non-financial assistance is still in development, because few of the standard types of programs have been able to prove that they are cost-effective. The standard approach involves training in general business skills, such as record-keeping, marketing, and managing money and inventory, often as a prerequisite to receiving credit. Such programs may be costly, and it has been difficult to confirm the extent to which they benefit microenterprises and microentrepreneurs. Recognition of this problem was partly responsible for the emergence of the minimalist credit methodology mentioned above, which A.I.D. strongly supports, and which largely eschews training and technical assistance.

On the other hand, A.I.D. has helped implementing organizations improve their methods of providing non-financial assistance in three ways:

- Concentrating technical assistance efforts in programs that work with business formation or transformation, where needs for new skills are strongest.
- Developing the capacity of organizations to provide standard types of training more cheaply and with better effect.
- Focusing assistance on the most binding constraints, such as markets and technical skills.

Under A.I.D.'s ARIES program, for example, Nathan Associates has reviewed training materials in use throughout the world, is adapting the best materials, and will make the new packages available to A.I.D. missions, U.S. PVOs and host country implementing organizations worldwide.

A.I.D. also is promoting a methodology known as subsector-based assistance that works on the market and technical constraints facing entrepreneurs in the same product line. This approach recognizes that tailors, for example, share common problems with other tailors that may have little relation to the problems faced by, say, street vendors. A recent study in Malawi found that tailors might face constraints because of import duties on cloth, competition from sellers of second-hand clothes, lack of access to large retail outlets, and lack of spare parts for sewing machines, among others. These are problems that neither credit nor training in general business skills will solve. A.I.D. has experimented with projects that address the needs of specific subsectors, working both directly with microentrepreneurs, and indirectly at levels that affect large groups of enterprises. A.I.D.'s most thorough effort to develop subsector-based assistance was the Central Java Enterprise Development Project (CJEDP) in Indonesia (see Box 3). Under the GEMINI project, A.I.D. will experiment with and promote subsector-based assistance with field missions, seeking to increase the now very small capacity to implement such potentially highly-leveraged programs.

C. Institutional Development

Because the microenterprise development field is still young, institutional capacity is often wanting, and varies greatly from one country to the next. A.I.D. has worked most frequently with local nongovernmental organizations, but there are other types of institutions, including governments, financial institutions, and business associations that could, with assistance, become more active in microenterprise development. Communications between programs has been limited, so that learning is a very slow

BOX 3. THE CENTRAL JAVA ENTERPRISE DEVELOPMENT PROJECT (CJEDP)

These examples illustrate how CJEDP worked (with A.I.D. funding) in two of its four subsectors.

1. New Technologies for Poor Shrimp Farmers. Along the north coast of Central Java, fish ponds are the primary source of food and income for more than 18,000 families, many of whom earn less than $250 per year. The method of the poorest pond farmers has been simply to capture and raise shrimp swept into the coastal ponds by the tides. With the shrimp market expanding, CJEDP saw a risk that these small and poor farmers could be squeezed out by large-scale operators using modern technology. The problem was not lack of credit assistance -- that had been tried and had failed -- but primitive methods.

CJEDP supported experiments by aquaculture experts to find ways for poor farmers to increase their yields without major up-front investments. It funded a local non-profit organization, Dian Desa, to carry out the work. Dian Desa developed a model hatchery to grow shrimp fry and sell them to the farmers -- a better source than the tides. It also created demonstration ponds, to show pond farmers how to raise more shrimp in the same body of water, and developed a nutritional shrimp feed that small farmers could afford to buy.

Dian Desa taught individual farmers how to use the new methods. When the first farmers produced yields more than triple their old harvests, other farmers signed up in great numbers. Now, after A.I.D. support has ended, Dian Desa continues to teach the new methods to small pond farmers, financing that outreach from the revenues produced by its hatchery.

2. Matching Products to Markets: The Metalworking Sector. In this sector, CJEDP acted as a broker for microenterprises and larger markets. Suyitno was one of a hundred or so skilled foundry men in the village of Ceper whose business had suffered from the closure of the railroad repair year years earlier. Like his father and his grandfather, Suyitno earned a meager living by casting scrap iron into crude implements.

One day, Suyitno was visited by Mr. Budi, a businessman from a neighboring city, who owned a factory that made simple machinery for bending and smoothing rattan poles. Budi thought that the small-scale foundry men in Ceper could produce some pieces of the machines more cheaply than he could, and he asked Suyitno to organize them and to oversee the casting of some samples. The samples were suitable, and orders came in regularly for more than two years. Suyitno's firm grew. He added new work space and several young employees. But then, as quickly as it began, the orders from Budi stopped. There was no apparent reason.

Suyitno turned for advice to Anton, the director of the metal subproject of CJEDP. Anton found that demand for the rattan machines had grown faster than anyone could have imagined and the market had expanded across the entire country. Unfortunately, Suyitno's frame parts could not pass the Department of Industry's new standards because of inferior molds used in casting them.

Anton met with Budi and Suyitno to find a solution. Suyitno believed that if the local founders could obtain aluminum molds, they could match the quality of the larger factory which was now supplying the products -- at a lower price. Anton proposed that the CJEDP project would supply these molds if Budi would pledge to continue to work with the local small producers to develop new products. CJEDP spent approximately $1,500 for molds that preserved the jobs and improved the capacity of 10 microenterprises.

process. A.I.D.'s institutional development activities are critical not only to A.I.D.'s ability to fund direct credit and training for entrepreneurs, but also for the development of strong microenterprise programs in developing countries that can attract support from other donors, governments, and the private sector. In 1989, 22 percent of all A.I.D.'s funding was used for institutional development. Approximately this level of commitment is expected to continue in 1990.

A large share of the funding that A.I.D. provides directly to U.S.-based PVOs and CDOs is used for institutional development. Typically, FVA/PVC grants enable PVOs to make the investment they need to develop new microenterprise programs. This support has been especially important for the socially-oriented PVOs, such as CARE and Catholic Relief Services, which historically have not served microenterprises. A.I.D. funding has helped such PVOs to "retool": to learn about microenterprise development, hire professional staff, design strategies, and train field staff and the staffs of their indigenous partner organizations. For PVOs primarily oriented toward microenterprise development, FVA/PVC support has provided room for experimentation that improves assistance methods.

A.I.D. has long supported central projects that seek to identify lessons of experience and disseminate them widely, including the PISCES, ARIES, and GEMINI projects. The teaching that these and other projects have done has involved a) widely circulated written documents; b) professional conferences and workshops both in the United States and in the field; c) direct technical assistance to A.I.D. missions and their projects; d) building a cadre of experts in microenterprise development; and e) providing opportunities for practitioners to learn from each other. Examples of the last item include support to the Small Enterprise Education and Promotion (SEEP) Network, which provides a forum for coordination and exchange of information among U.S. PVOs and their affiliates, and the development under ARIES of teaching cases on strategic management and credit management. These products provide vehicles for practitioners to learn from each other.

Two of the approaches to microenterprise development that A.I.D. finds most promising have intensive requirements for institutional strengthening:

- Achieving financial self-sufficiency and expansion in credit programs is very difficult. Existing institutions have to restructure, and new institutions must begin on a businesslike footing. In Honduras, for example, A.I.D. is funding a full-time advisor to help its microenterprise program grantees to computerize their credit operations, an essential prerequisite to cost reduction in programs that hope to reach large numbers of borrowers with small loans.

- Subsector-based assistance will require the development of new analytical and practical skills among implementing organizations, as well as new institutional structures.

D. The Supportive Environment: Policy and Regulatory Reform

Through its work in policy and regulatory reform, A.I.D. encourages governments to create an operating environment that is supportive of microenterprise development. Economic policy and government regulations create two related, but distinct aspects of that environment. Because much of A.I.D.'s work in these areas is negotiated through complex non-project assistance agreements, it is difficult in most instances to attribute specific amounts of funding directly to microenterprise assistance. Accordingly, although only $3.6 million in 1990 funding will be devoted specifically to microenterprise policy reform, many elements of much larger reform programs will lead to improvements in the environment in which microenterprises operate.
In the realm of economic policy, microenterprises must often contend with a system that has been established to promote large, capital-intensive, import substitution businesses. A.I.D. typically attempts to persuade governments to dismantle these protection systems, which hurt the economy as a whole, because they gobble up large implicit and explicit subsidies. A.I.D. recommends steps such as reducing the flow of subsidized credit into large businesses, and freeing access to imported spare parts and raw materials. Such steps make it easier for small-scale and microenterprises to compete for access to resources. These efforts are supplemented by research that identifies problems specific to microenterprises, as illustrated in Box 4.

In the area of government regulations, as Hernando de Soto has pointed out, the relationship between state and private enterprise in many countries is not healthy: the state wants to control business activity rather than to provide a level playing field.[23] To avoid regulations that would ruin their businesses, the poor are forced to direct their entrepreneurial energies through informal channels.

Informality, however, often raises the costs of doing business and inhibits growth. For example, lack of secure property rights denies the use of property as collateral for obtaining loans, and the inability to enforce contracts constrains the formation of partnerships and the sharing of facilities and technologies. Police harassment often results in bribes that directly reduce profits and incomes among the poor. A.I.D. believes it crucial to change the state-business relationship to make formality easier to achieve, and to reduce the costs of being informal. A.I.D. supports the development of

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[23] Hernando de Soto, The Other Path: The Invisible Revolution in the Third World, New York: Harper and Row, 1989.

BOX 4. THE VALUE OF INDIRECT ASSISTANCE:
THE TRADITIONAL BEER BREWERS OF BOTSWANA

A.I.D. has found ways to influence whole groups of microentrepreneurs, by working indirectly. A simple study and the actions that followed from it led to striking improvements in the livelihoods of the thousands of home-based sorghum beer brewers in Botswana.

Sorghum beer is a thick, bitter drink that provides a major source of calories in a country with an often inadequate diet. Women, living in poverty on the barren plains, brew the beer at home, to pay for the few products they must buy rather than make themselves.

A.I.D. supported an analysis of the market for traditional beer. The study examined possible competition from factory brews, and ways to make home-based production more profitable. The analyst, who worked with the Government of Botswana, brought some far-reaching facts to light. First, by showing how many lives depended on the income from beer brewing, he helped convince the government not to approve a new factory in Botswana that would have squeezed out the traditional brewers. Second, he found that brewers who used commercially produced malt as an input had higher incomes than those who made the malt themselves. In response, the Ministry of Commerce and Industry launched an educational campaign to encourage brewers to use commercial malt. Finally, the analyst found that local authorities were harassing home brewers, at least partly because of the undue influence of the competing factory brewers. The government took action to end the harassment.

Each of these steps was very important to the home brewers. Their incomes rose, and their futures were protected. The analysis A.I.D. sponsored, and the steps the Government took in response, cost little, especially in comparison to the number of people whose enterprises they touched.

indigenous institutions that can engage in dialogue directly with the government, such as de Soto's Institute for Liberty and Democracy (ILD) in Peru. In fact, A.I.D. has provided a grant to ILD to enable it to act as a worldwide resource institution, to spread its approach and methodology throughout the developing world. Delegations from several countries in both Asia and Africa have visited the ILD for training. These visits are intended to spark actions in the visitors' home countries.

Taking this concept one step further, a new project, Institutional Reform and the Informal Sector (IRIS) is now under design, and will begin in the summer of 1990. The IRIS project will support developing country organizations in identifying the legal, institutional, and administrative impediments enterprises face and in developing strategies for correcting these deficiencies. Support will take the form of collaborative research between U.S. and indigenous institutes, training, promotion of direct interaction between such institutes in different countries, and support to increase the capacity of these institutes to administer effective research and advocacy programs.

E. Markets

As described in Part I of this report, the most important condition for the success of microenterprises is growth of their markets. Given the nature of microenterprise markets, growth requires increasing purchasing power among poor consumers. A.I.D. works with host governments to promote nationwide economic growth through structural adjustment and policy reform. Equally important in this context, A.I.D. has long provided assistance that increases the purchasing power of exactly the kinds of poor consumers microenterprises serve.

General efforts to expand markets are not classified as part of the microenterprise program, because they foster a wide variety of benefits, with microenterprise growth one happy by-product. Nevertheless, a strong link exists between A.I.D.'s support to small farmers and its microenterprise activities. Small farmer development has been one of the foundations of A.I.D.'s approach to economic development for at least two decades. In many ways, the interest in microenterprises grew out of the realization by those who studied small farmers of the multitude of non-farm entrepreneurial activities that took place in small towns and rural areas, and out of a desire to understand the mutually supportive relationship between farmers and other entrepreneurs. As a result, A.I.D. has always defined microenterprises as non-agricultural activities. However, some observers prefer to make no distinction between the two, as the people involved in them are often the same. If A.I.D. were to adopt a definition of microenterprise that included micro-farmers, it would be able to show hundreds of millions of dollars in microenterprise credit each year, because it continues to sponsor major programs of small farmer credit throughout the world.

PART III. A.I.D.'S NEW MICROENTERPRISE PROGRAM

The past two years have provided A.I.D. an opportunity to take stock of its various microenterprise activities, both to develop a better picture of the scope and nature of its investments, and to gain an improved understanding of the most effective ways to work in this field. With that important preparation, A.I.D. is now poised to meld its activities into a more comprehensive microenterprise program, and indeed, has already taken several steps to do so. While budget constraints and earmarking mean that the total amount of resources going into microenterprise development cannot expand significantly, their consolidation into a more visible and systematic program will mean that those resources will be used more effectively, and will carry greater benefit to the poor. A.I.D. is pleased to take this opportunity to describe the program.

A. Direct Financial Support to Microenterprise Programs

The heart of the program will, of course, be the funding A.I.D. provides directly to microenterprise projects, primarily through field missions. Through this funding, A.I.D.'s objective will be to build strong, sustainable microenterprise programs in host countries, programs that will benefit the poor substantially, both in the near term and into the future. A.I.D. will continue to apply its funding to a diverse set of activities that address the four basic business needs, as well as the requirements of institutional development needed to support direct assistance. However, as part of the new program, it proposes to promote greater emphasis, including increasing annual funding, on three types of programs:

1) credit programs that use a minimalist credit methodology;

2) experimental forms of non-financial assistance; and

3) regulatory reform activities.

These are the types of programs that have shown the greatest promise in recent years for sustainably improving the performance of microenterprises. Increasing the share of microenterprise assistance devoted to these activities will require an internal effort of promotion and education with A.I.D. staff and the staffs of organizations A.I.D. works with. This promotional effort is an important aspect of the new program, as described below.

Another important part of A.I.D.'s funding will come through the Office of Private and Voluntary Cooperation (FVA/PVC) for activities carried out by PVOs and cooperative development organizations. FVA/PVC has actively encouraged U.S.-based organizations to work in microenterprise development, and has worked closely with several traditionally relief-oriented PVOs to create and strengthen their microenterprise programming capacity. It also has promoted participation by cooperative development organizations in microenterprise development, including innovative pilot efforts such as the recent grant to the World Council of Credit Unions and the National Cooperative Business Association to improve credit unions' services to microentrepreneurs. FVA/PVC is now assisting several PVOs to gain experience with "village banking" programs. FVA/PVC encourages new grant proposals for microenterprise activities. With the help of the GEMINI project, FVA/PVC will work to build the capacity of U.S. PVOs, and through them to help improve programs administered by their partner organizations in the field. PVC has a long-term commitment to invest in PVOs' technical and management capabilities in microenterprise development, working in collaboration with mission funding of U.S. and local PVOs.

Finally, A.I.D. plans to continue its close working relationship with the Peace Corps' microenterprise program, because it complements the agency's efforts to reach the poor, increase incomes, and generate jobs. The Microenterprise Development Program (MEDP), described earlier, will be extended through at least 1992. MEDP combines the human resources of the Peace Corps with A.I.D.'s financial resources to achieve greater effect from both. Several new countries will be brought into the program. The future focus of this collaboration will be the development of local institutions that serve the business growth needs of very small enterprises in the communities in which Peace Corps volunteers work. A.I.D. will provide extended support for training of volunteers and their local counterparts, the creation and use of innovative training materials, and workshops and conferences to reach poor business men and women.

The kind of program A.I.D. wishes to pursue involves experiments in many countries, as is reflected by the current dispersion of the microenterprise program in 47 countries. In the near term A.I.D. proposes to maintain mission and central bureau programming near its current level. Although A.I.D. would like to be able to expand the microenterprise program, the realities of its budget prevent this. Limitations include the geographic concentration of A.I.D. funds, particularly in countries where most U.S. assistance is structured in a way that precludes its use for microenterprise development, such as Eastern Europe. At the same time, discretionary development assistance funds are being reduced for countries that are not in the political spotlight. In some countries, where strong institutional capacity is lacking, it is difficult, even unwise, for A.I.D. to spend too much on microenterprise development simply because it has funds available. In future years, as institutional capacity grows in host countries and as budget constraints may ease, A.I.D. hopes to be able to expand its microenterprise program more significantly.

B. Support for the New Program

Turning a disparate set of activities into a focused program will require an agency-wide effort of promotion, education and coordination, which A.I.D. is prepared to undertake. The real action on microenterprise development must take place in field missions, where new projects are shaped. Missions need support in order to build their own capacity to design and implement better microenterprise projects. A.I.D./Washington has set the stage for mission support by creating a new Office of Small, Micro and Informal Enterprise Development within the Bureau for Private Enterprise to take the lead in coordinating and implementing the program. That office will be responsible for the various elements of the program, including the GEMINI project, the Peace Corps program, the microenterprise monitoring and information system, liaison with A.I.D.'s Advisory Committee on Microenterprise Development, and coordination of microenterprise field projects within the agency.

At the same time, the regional bureaus will be asked to place increased emphasis on the microenterprise activities of their regions. The Africa Bureau has already done this, by funding a regional advisor whose task is to work with Africa field missions specifically in the area of microenterprise development. That advisor already is well into the process of helping missions move from a "target of opportunity" approach to microenterprise assistance to a more holistic approach that considers all four basic business needs of microenterprises, as stated previously. The other two regional bureaus will be encouraged to establish similar positions as needed.

The GEMINI project will assist A.I.D.'s regional bureaus and field missions to implement the new program and promote more effective support for microenterprise development. As a research project, it will be GEMINI's task to search for lessons about the needs of microenterprises and about how best to assist them. As a service project, GEMINI will communicate these lessons throughout the microenterprise development community, both within A.I.D. and outside it. In particular, GEMINI will conduct a major program of action research on the expansion and promotion of minimalist credit programs. This action research will examine how large, financially self-sufficient programs are built, and will help individual credit programs to put those findings into action. It will also conduct an action research program on experimental approaches to non-financial assistance, including interventions that focus on the needs of particular subsectors and on indirect methods of assistance. The findings of these and other action research programs will be disseminated widely both throughout A.I.D. and among its cooperating agencies through conferences, seminars and workshops, both in the U.S. and in the field.

A.I.D. will continue to sponsor workshops, both in the field and in Washington, to ensure that agency staff as well as host country institutions are kept informed of the latest developments in microenterprise practice. These workshops will promote direct contacts between practitioners in developing countries, so that practical experience can be transmitted directly. A.I.D. also believes that practitioners should learn from the examples of the most successful microenterprise projects, and accordingly, it will support cross-visits by practitioners to such projects.

In order to be sure that the new microenterprise program is achieving its objectives, A.I.D. will continue to need the advice of an independent committee of experts, such as the Advisory Committee on Microenterprise. Indeed, the program described in this section reflects suggestions made by the Committee in February, 1990.

Finally, implementation of a new monitoring system, as described in Part IV, will enable A.I.D. to have the information needed to effect improvements in field-based microenterprise activities. It is, therefore, an important aspect of the new program.

PART IV. MONITORING AND EVALUATION NEEDS OF A.I.D.'S MICROENTERPRISE PROGRAM

A.I.D. recognizes the need to establish an agency-wide system to monitor both the level and characteristics of its microenterprise development activities. Until now, A.I.D. has measured its microenterprise activities only through ad hoc surveys or through the annual budget process. The budget process provides information on obligation levels, but not on program characteristics or impacts. Moreover, the budget system is based on projects which often encompass a wide range of activities, only some elements of which relate to microenterprise development.

The budget process alone will not suffice as a monitoring system. Accordingly, A.I.D. has directed the GEMINI project to assess the feasibility of establishing a comprehensive monitoring system for the microenterprise program. That preliminary feasibility study is now underway. This section gives a summary of findings to date. A final feasibility study, including cost estimates, is epected to be completed in April, 1990.

A. Potential Uses of a Monitoring System

A monitoring system for A.I.D.'s program will require three levels of participation: grantees, A.I.D. missions, and A.I.D./Washington. Each will bear significant costs in maintaining and operating such a system, and therefore, each should have a use for the information the system produces. The three levels can be thought of as a pyramid with the implementing organizations at the base, followed, an ascending order, by the A.I.D. missions, A.I.D./Washington and, finally, the Congress and the public at large. Information needs at each level depend on the types of decisions made there. These decisions are of an increasingly general nature as we ascend the pyramid. Because of the cooperative nature of links between levels, any system will depend on maintenance of good working relationships throughout.

At the foundation of this pyramid, the implementing organizations require information necessary to run their programs and maintain institutional health. The natural operating processes of the organizations generate such information. For example, data on clients are recorded upon application for assistance, and checks written leave a record of loans made. An effective monitoring system will be built upon the information that these natural operating processes generate.

At the next level up, the A.I.D. missions must determine how microenterprise activities should fit into their overall country programs. They need data on program impact, the competence of implementing organizations they support, and the sustainability of project activities.

A.I.D./Washington must decide how strong an emphasis to place on microenterprise development relative to other types of programs, and what kinds of microenterprise programs to support. To make these decisions it needs information both on the magnitude and characteristics of the activities it funds, and on the costs and benefits of various types of programs.

Finally, Congress needs to be informed on whether its statutory requirements are being met, and on the development impact of microenterprise programs.

In simplest terms, the monitoring system must be useful to all those involved in carrying it out. Furthermore, it must build from the specific to the general, grounded in the operating processes of implementing organizations. Several complicating factors make this simple concept somewhat more complex in reality.

Very few of the implementing organizations that work with microenterprises currently have management information systems that could provide the kinds of information needed. Typically, they maintain data on outputs such as loans made, or people trained, but less frequently on beneficiary characteristics, and rarely on impacts, such as resulting growth in employment. Moreover, systems at the grantee level are unique to each organization, so that data cannot easily be aggregated across programs. A major effort to upgrade organizational capability would be required before genuinely reliable data on program performance and impact could be collected. Standardization would have to be an essential part of the upgrading effort, so that the data could feed into the central system. Although the upgrading process would be a long and costly one, it could well bring significant benefits to implementing organizations through improved management.

An issue at the A.I.D. mission level is that while a system to track compliance with an earmark must follow the logic of the federal budget process, data on program characteristics and performance cannot easily be made to conform to that logic. For example, many lenders use A.I.D. funds to make several short term loans within a year. Should they report the gross or only the net activity? How should exchange rate fluctuations during the year be treated? Similar quandaries abound. Fortunately, there is no real need to force programs into the budget system, when two separate but complementary tracking systems could be developed. The budget tracking system could be fully completed by A.I.D. missions, while program tracking would require input from implementing organizations. In addition, some relevant information must be brought in from still other sources. For example, the system should incorporate national demographic data on income distribution so that the poverty level of beneficiaries can be accurately interpreted.

At the A.I.D./Washington level, it is most useful to have data in virtually raw form, to support in-depth, flexible data analysis. Raw data reporting should also be easiest for implementing organizations.

Developing and implementing the kind of monitoring system implied by these considerations would require strong leadership from A.I.D. The process necessarily involves a large number of people throughout the agency and its grantees, all of whom would have to be committed to the system in order to make it work. It would also take some time to implement, and would not be expected to reach its full potential until it had been tested and refined over the course of several reporting cycles. The monitoring systems used in the A.I.D. population and child survival programs, which require several million dollars annually to maintain, attest to the magnitude of the effort required. They also attest that reliable data can demonstrate real impact in the areas the programs address. Continued financial support for microenterprise activities will inevitably depend on such demonstration of impact. Although decisions about the scope and nature of a monitoring remain to be made, A.I.D. is committed to developing a system that will meet information requirements at all levels as nearly as is possible.

Annex Table 1.
Annual Activity Levels
Summary of Obligations, by Region and Country
(US $000)

Region and Country	No.	1988	1989	1990	LOP
Region: Central					
ACCION International	1	218	211	338	767
Save the Children	1	256	302	323	881
CARE	1	426	364	425	1,215
World Relief Corp.	1	474	468	719	1,661
CRS	1	-	58	273	331
Coop. Housing Fund	1	-	110	-	110
Foster Parents Plan	1	686	681	678	2,045
Opportunity Int	1	450	450	450	1,351
Technoserve	1	837	602	457	1,896
Intl Voluntary Svcs	1	141	86	109	336
WOCCU	1	-	30	30	60
OEF	1	471	532	478	1,481
	12	3,959	3,894	4,280	12,134
egion: Asia/Near East					
Egypt	1	128	322	3,063	-
Morocco	1	62	-	-	84
Jordan	1	-	-	582	3,200
Yemen	5	-	40	590	15,600
Nepal	3	-	132	1,347	5,311
Sri Lanka	7	1,156	5,260	2,115	13,527
Bangladesh	1	200	200	-	1,037
Pakistan	3	2,425	2,830	3,175	15,500
South Pacific	8	1,810	2,690	1,570	8,175
Philippines	5	1,840	6,658	2,378	14,195
Thailand	2	478	650	262	1,390
Indonesia	7	11,723	6,722	5,940	47,887
	44	19,822	25,504	21,022	125,906
Region: Latin America and Caribbean					
Belize	4	625	50	700	3,210
Bolivia	1	-	-	1,193	-
Costa Rica	2	1,500	1,958	1,699	6,680
Dominican Republic	5	401	298	1,062	1,332
Ecuador	2	625	521	744	1,490
El Salvador	13	1,064	5,792	4,351	11,731
Guatemala	6	3,826	3,306	5,103	12,796
Haiti	2	898	625	715	4,686
Honduras	6	7,118	2,623	4,476	21,737
Paraguay	1	80	70	-	350
Peru	3	546	507	969	4,436
Jamaica	13	1,660	3,434	1,528	10,243
RDO/Caribbean	1	1,641	1,451	470	6,229

Chile	1	-	128	102	300
Colombia	2	116	128	141	879
	62	20,100	20,891	23,253	86,099
Region: Africa					
Zambia	1	-	500	1,114	4,187
Malawi	4	1,400	5,579	5,817	23,621
Zimbabwe	4	2,500	2,500	3,141	33,051
Kenya	6	666	3,331	4,029	20,551
Lesotho	4	1,083	1,074	968	4,686
Botswana	3	110	610	660	2,130
Sierra Leone	1	-	44	58	744
Swaziland	1	-	-	250	250
Sudan	1	-	402	624	1,026
Zaire	1	50	250	200	1,500
Liberia	1	1,100	1,600	2,700	5,400
South Africa	1	2,300	905	-	5,630
Chad	1	494	555	396	1,446
Niger	1	243	1,340	1,340	5,900
Senegal	5	1,300	6,679	2,250	24,779
Madagascar	4	1,056	2,170	2,863	7,868
Mali	4	398	1,357	2,347	8,134
Southern Africa Reg.	3	700	1,254	2,832	5,021
Togo	5	548	567	2,435	13,850
Rwanda	1	1,000	90	985	-
	52	14,948	30,807	35,009	169,774
GRAND TOTAL	170	58,829	81,096	83,564	393,913

Annex Table 2.
Program Types
Summary of Obligations, by Region and Country, 1989
(US $000)

Region and Country	No.	Loans	T/TA	InSp	P/REG	Other	Total
Region: Central							
ACCION International	1	-	-	211	-	-	211
Save the Children	1	40	80	-	-	182	302
CARE	1	17	17	322	-	8	364
World Relief Corp.	1	136	105	227	-	-	468
CRS	1	-	25	33	-	-	58
Coop. Housing Fund	1	-	-	-	110	-	110
Foster Parents Plan	1	122	157	-	219	183	681
Opportunity Int	1	114	28	179	-	129	450
Technoserve	1	-	383	64	155	-	602
Intl Voluntary Svcs	1	-	86	-	-	-	86
WOCCU	1	-	20	5	5	-	30
OEF	1	-	44	77	9	402	532
	12	429	945	1,118	498	904	3,894
Region: Asia/Near East							
Egypt	1	141	-	181	-	-	322
Morocco	1	-	-	-	-	-	-
Jordan	1	-	-	-	-	-	-
Yemen	5	-	-	10	30	-	40
Nepal	3	28	54	50	-	-	132
Sri Lanka	7	593	1,670	150	100	2,747	5,260
Bangladesh	1	58	50	45	-	47	200
Pakistan	3	-	1,130	200	-	1,500	2,830
South Pacific	8	-	865	1,825	-	-	2,690
Philippines	5	1,820	2,457	2,087	46	248	6,658
Thailand	2	39	51	-	-	560	650
Indonesia	7	2,437	1,191	181	-	2,912	6,722
	44	5,116	7,468	4,729	176	8,014	25,504
Region: Latin America and Caribbean							
Belize	4	-	50	-	-	-	50
Bolivia	1	-	-	-	-	-	-
Costa Rica	2	864	769	325	-	-	1,958
Dominican Republic	5	150	-	148	-	-	298
Ecuador	2	451	70	-	-	-	521
El Salvador	13	5,531	197	64	-	-	5,792
Guatemala	6	3,185	22	99	-	-	3,306
Haiti	2	408	143	73	-	-	625
Honduras	6	1,550	822	251	-	-	2,623
Paraguay	1	-	70	-	-	-	70
Peru	3	298	194	4	5	6	507
Jamaica	13	1,950	20	394	-	1,070	3,434
RDO/Caribbean	1	818 49	83	550	-	-	1,451

Chile	1	-	-	128	-	-	128
Colombia	2	10	57	61	-	-	128
	62	15,215	2,497	2,097	5	1,076	2[illegible]91

Region: Africa

Zambia	1	-	250	250	-	-	500
Malawi	4	840	708	2,041	1,990	-	5,579
Zimbabwe	4	-	1,500	1,000	-	-	2,500
Kenya	6	744	853	1,627	74	33	3,331
Lesotho	4	374	416	284	-	-	1,074
Botswana	3	350	200	45	-	15	610
Sierra Leone	1	16	21	-	-	7	44
Swaziland	1	-	-	-	-	-	-
Sudan	1	222	180	-	-	-	402
Zaire	1	-	150	100	-	-	250
Liberia	1	1,000	300	300	-	-	1,600
South Africa	1	100	-	585	220	-	905
Chad	1	-	132	423	-	-	555
Niger	1	140	1,200	-	-	-	1,340
Senegal	5	3,300	1,200	2,079	-	100	6,679
Madagascar	4	2,118	52	-	-	-	2,170
Mali	4	76	948	-	333	-	1,357
Southern Africa Reg.	3	-	-	815	439	-	1,254
Togo	5	214	182	171	-	-	567
Rwanda	1	-	90	-	-	-	90
	52	9,494	8,382	9,720	3,056	155	30,807
GRAND TOTAL	170	30,254	19,292	17,664	3,735	10,149	8[illegible]96

Annex Table 3.

Microenterprise Funding Patterns, by Region: 1988

Amounts in US $000

	Central	ANE	LAC	AFR	Total
Loans	362	3,115	10,279	4,678	18,434
Training and TA	1,283	8,651	2,248	3,168	15,350
Instit. Support	1,155	2,303	6,663	4,043	14,165
Policy Reform	362		277	1,543	2,182
Other	797	5,754	634	1,515	8,700
Total	3,959	19,823	20,101	14,948	58,831

Percentage Allocation of Funds

	Central	ANE	LAC	AFR	Total
Loans	9.1	15.7	51.1	31.3	31.3
Training and TA	32.4	43.6	11.2	21.2	26.1
Instit. Support	29.2	11.6	33.1	27.0	24.1
Policy Reform	9.1		1.4	10.3	3.7
Other	20.1	29.0	3.2	10.1	14.8
Total	100.0	100.0	100.0	100.0	100.0

Microenterprise Funding Patterns, by Region: 1989

Amounts in US $000

	Central	ANE	LAC	AFR	Total
Loans	429	5,116	15,215	9,495	30,255
Training and TA	945	7,469	2,498	8,383	19,294
Instit. Support	1,118	4,729	2,098	9,720	17,666
Policy Reform	498	176	5	3,056	3,735
Other	904	8,014	1,076	155	10,149
Total	3,894	25,504	20,892	30,809	81,099

Percentage Allocation of Funds

	Central	ANE	LAC	AFR	Total
Loans	11.0	20.1	72.8	30.8	37.3
Training and TA	24.3	29.3	12.0	27.2	23.8
Instit. Support	28.7	18.5	10.0	31.6	21.8
Policy Reform	12.8	0.7	0.0	9.9	4.6
Other	23.2	31.4	5.2	0.5	12.5
Total	100.0	100.0	100.0	100.0	100.0

Microenterprise Funding Patterns, by Region: 1990

Amounts in US $000

	Central	ANE	LAC	AFR	Total
Loans	475	4,657	17,131	14,111	36,374
Training and TA	1,408	5,201	2,694	9,508	18,810
Instit. Support	1,358	5,217	3,053	7,248	16,876
Policy Reform	331	672	106	2,516	3,625
Other	708	5,275	271	1,377	7,631
Total	4,280	21,022	23,255	35,009	83,566

Percentage Allocation of Funds

	Central	ANE	LAC	AFR	Total
Loans	11.1	22.2	73.7	40.3	43.5
Training and TA	32.9	24.7	11.6	27.2	22.5
Instit. Support	31.7	24.8	13.1	20.7	20.2
Policy Reform	7.7	3.2	0.5	7.2	4.3
Other	16.5	25.1	1.2	3.9	9.1
Total	100.0	100.0	100.0	100.0	100.0

Microenterprise Funding Patterns, by Region: LOP

Amounts in US $000

	Central	ANE	LAC	AFR	Total
Loans	1,266	20,717	52,284	49,784	124,051
Training and TA	3,637	41,546	12,350	58,453	115,985
Instit. Support	3,631	19,123	17,699	48,628	89,081
Policy Reform	1,191	2,056	488	9,769	13,504
Other	2,409	39,966	2,223	2,891	47,489
Total	12,134	125,907	86,100	169,776	393,916

Percentage Allocation of Funds

	Central	ANE	LAC	AFR	Total
Loans	10.4	16.5	60.7	29.3	31.5
Training and TA	30.0	33.0	14.3	34.4	29.4
Instit. Support	29.9	15.2	20.6	28.6	22.6
Policy Reform	9.8	1.6	0.6	5.8	3.4
Other	19.9	31.7	2.6	1.7	12.1
Total	100.0	100.0	100.0	100.0	100.0

IESC'S PRIVATE ENTERPRISE ENVIRONMENT REPORT

Mr. Obey. At this point we will include in the record the International Executive Service Corps report on the Private Enterprise Environment requested in the fiscal year 1990 report.

[IESC's Private Enterprise Environment Report follows:]

IESC
INTERNATIONAL EXECUTIVE SERVICE CORPS
8 STAMFORD FORUM, STAMFORD, CONNECTICUT
TELEPHONE (203) 967-6000
TELEX 4750174 (INTEXUI)
FAX (203) 324-2531

MAILING ADDRESS P O BOX 10005
STAMFORD CONNECTICUT 06904-2005

April 19, 1990

The Honorable Thomas S. Foley
Speaker
U.S. House of Representatives
8204 U.S. Capitol
Washington, DC 20515

Dear Mr. Foley,

This is in response to the request contained in the report from the Committee on Appropriations to the Senate on H.R.2939 FOREIGN OPERATIONS, EXPORT FINANCING, AND RELATED PROGRAMS APPROPRIATION BILL, 1990.

The request on page 110 of the report is as follows:

> "The Committee further requests that by April 30, 1990, IESC report to the President and to the Congress its assessment of the private enterprise environment in the countries within the scope of its activities and its view of the opportunities for effective IESC projects in those countries."
>
> "The Committee has used the occasion of the 25th anniversary of IESC to review the Corps' past performance and its future potential. It concludes that in the area of free enterprise, IESC is one of the cost-effective foreign assistance instruments available to the United States."

Examination of these two points (1. assessing the environment for private enterprise and 2. opportunities for effective projects) is discussed in detail for each country in the attached report. In briefest terms, however, we comfortably conclude:

1A) The environment for private enterprise has continued to improve. For example, IESC is doing twice as many projects now than it did in 1983. This is significant because we charge our clients for the service so the growth represents real demand not merely acceptance of a giveaway.

This growth is shown on Chart I attached.

1B) Since IESC began 25 years ago, thirteen other industrial nations now have IESC-type organizations. Despite the competition from other nations' senior services, the market for IESC projects continues to grow.

The Hon. T.S. Foley
U.S. House of Representatives
Page 2
April 19, 1990

2A) Opportunities for effective use of IESC projects abound. Chart II shows the results after a project has been completed. As you can see, one of three clients reinvests in his business, often buying American-made equipment. One in seven wants a joint venture with a U.S. company. We arrange these. Moreover, as businesses improve many new jobs are created.

2B) Finally, the cost per project has been reduced significantly both in total costs and in that portion provided by A.I.D. Charts III and IV. A.I.D. provided about 60% of total funding of $14,954,940 in 1989, the balance coming from clients and from U.S. corporations, foundations and individuals. In addition to the funding, the value of volunteer executives as calculated by Price Waterhouse was $20,172,939.

We have been active in Hungary with 21 projects started, five more in the works. In Poland three projects have started, 10 are in the works. Expenses of these projects have been borne by the Hungarian and Polish clients with help from U.S. foundations.

We have now received verbal assurance from PRE/A.I.D. that in FY 90 we will receive $300,000 for basic IESC projects and $230,000 for Trade and Investment Services in Hungary and Poland. This will help meet the IESC commitment to services to private enterprise in Eastern Europe. IESC also has received requests from Yugoslavia, Czechoslovakia and, in the Soviet Union, from Estonia, Latvia and other areas.

In short, the environment for private enterprise definitely is warmer and larger. Opportunities to be effective are many, only limited by the funds made available to IESC.

As requested, this report is also being sent to Mr. George Bush, President of the United States; and Mr. J. Danforth Quayle, President of the Senate.

Sincerely,

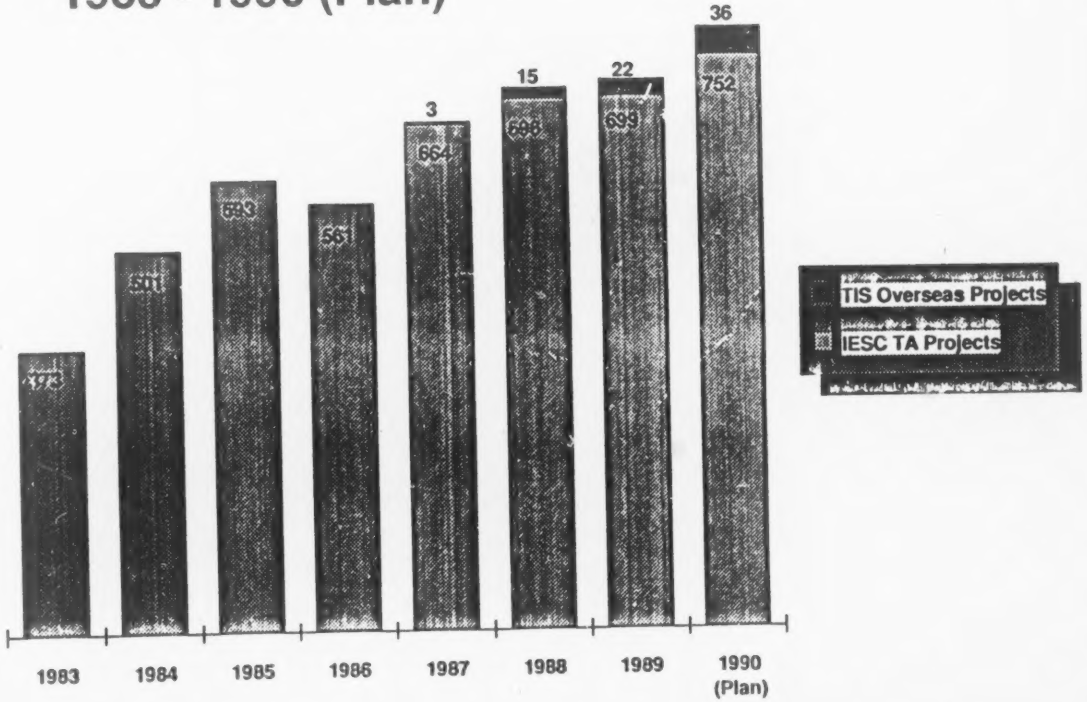
Tom

Thomas S. Carroll
President and CEO

TSC:ed
1218T
Enclosures

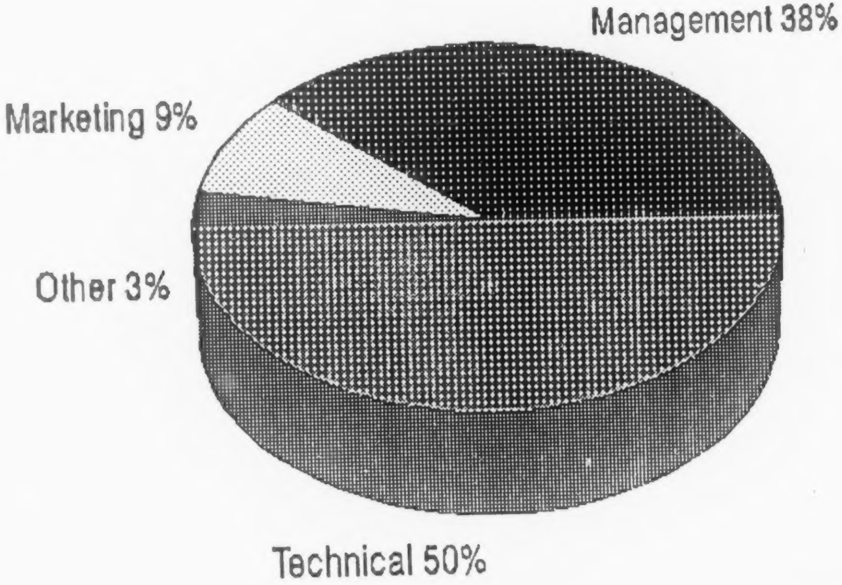
I

TOTAL PROJECT STARTS
1983 - 1990 (Plan)



II
RESULTS

Client Assistance Review Categories



II

Marketing Category : *Highlights*	
Question to Client	% Answering "YES"
Sales Increased	50.0%
Profits Increased	40.9%
Capital Investments Made	36.4%
Client Considering Joint Venture	13.6%
Jobs Created	59.1%
Overall Improvement in Workers' Skills	63.6%
Employee Attitudes Improved	59.1%
Management/Employee Relations Improved	40.9%
Employees Offered Better Salary Incentives	27.3%
Improved Management Information Systems	77.3%
Attitudes of Management	54.5%
Attitudes of Workers	45.5%
Attitudes of Senior Executives	68.2%

II

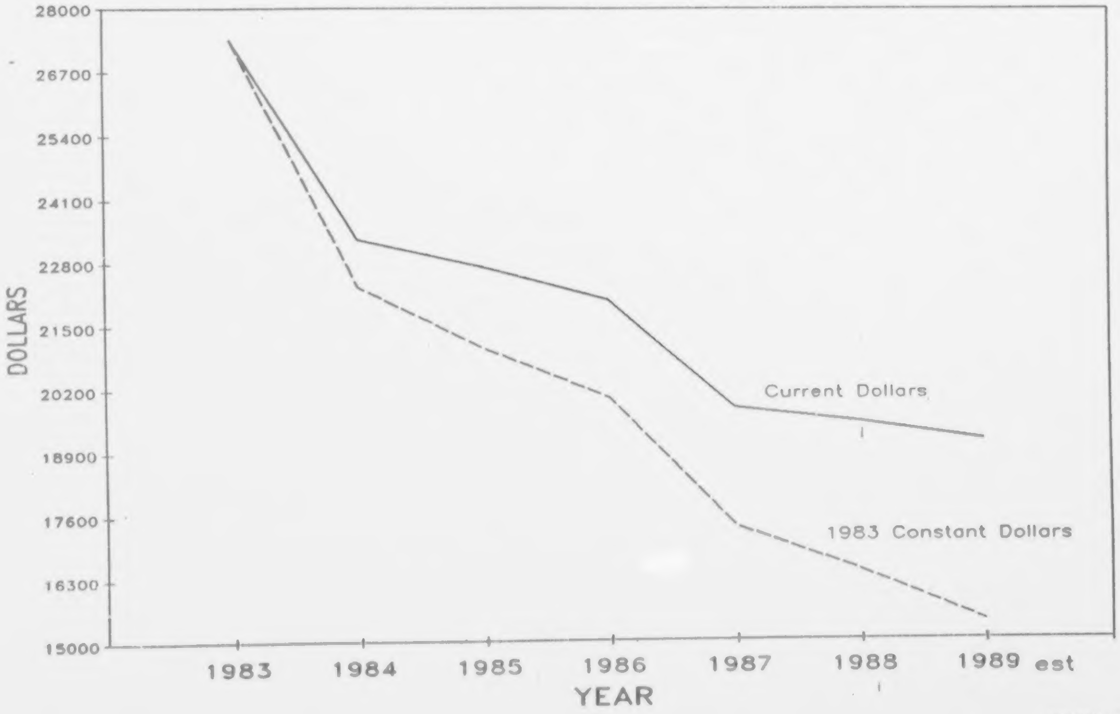
Technical Category : *Highlights*

Question to Client	% Answering "YES"
Output Increased	58.9%
Quality Control Program Improved	72.9%
Product Quality Improved	74.4%
Waste Reduced	48.8%
Downtime of Equipment Reduced	32.6%
New Marketing Programs Developed	29.5%
Unit Costs Decreased	34.9%
New Parts/Tools/Equipment Purchased	48.8%
U.S. Purchase of Equipement	28.4%
Machinery Maintenance Improved	46.5%
New Procedures or Processes Introduced	73.6%
Plant Operations Improved	66.7%
Suppliers Benefitted From the IESC Program	28.7%
Hard Currency Savings/Earnings Were Made	20.2%

International Executive Service Corps
P.O. Box 10005,
Stamford, Connecticut 06904-2005

III

Total Project Expenses
(per project)



projcpl2 2/90

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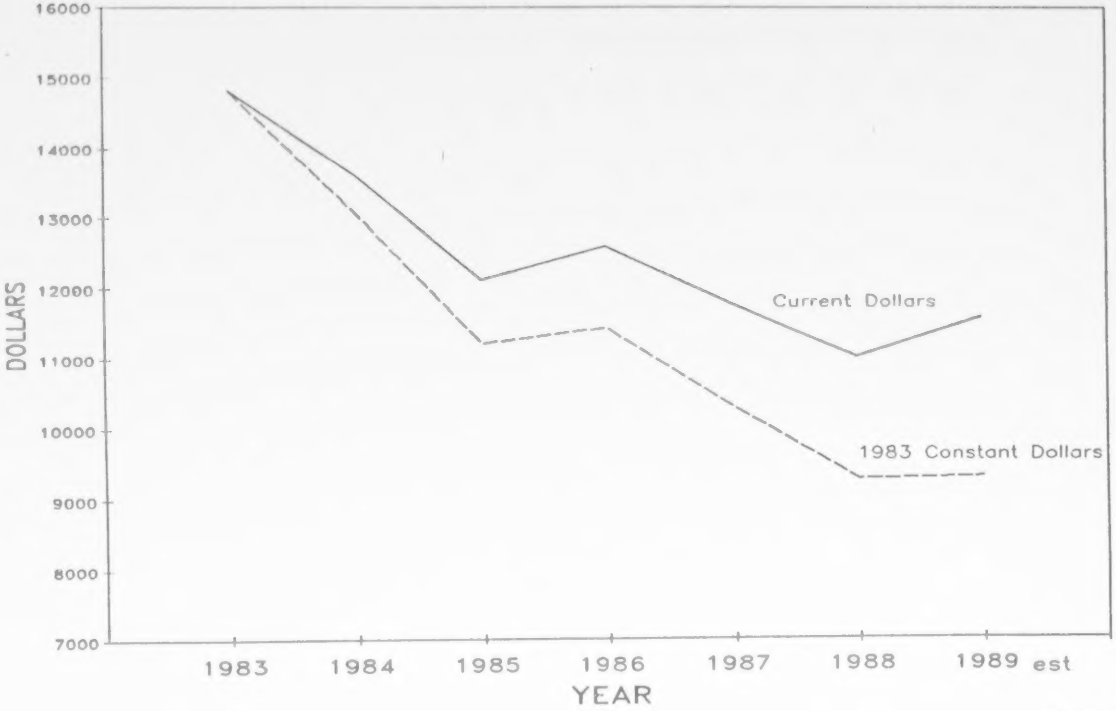
P.O. Box 10005,
Stamford, Connecticut 06904-2005

IV

Cost to AID (per project)



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INTERNATIONAL EXECUTIVE SERVICE CORPS REPORT ON PRIVATE ENTERPRISE ENVIRONMENT

This report will describe the private enterprise environment of each country where IESC has an office. Opportunities for IESC projects also are assessed by the IESC Country Director. The report is categorized by region.

CENTRAL AMERICA AND THE CARIBBEAN

GUATEMALA

Private Enterprise Environment

Guatemala's economy is dominated by the private sector, which generates nearly 90 percent of Gross Domestic Product (GDP). The government's participation in the productive process is limited largely to public utilities, and several development-oriented financial institutions. The government, however, continues to exercise a significant regulatory role.

Agriculture is the dominant economic activity, contributing about a quarter of GDP and accounting for more than three-fourths of exports. There has been an upward swing in textile, apparel and non-traditional agriculture exports to industrialized country markets (especially the United States). New export promotion laws adopted by the Guatemalan Congress have provided fiscal incentives for investments in non-traditional export industries.

Opportunities for IESC Projects

A greater demand for technical assistance, new technology and new capital goods has resulted from the Guatemalan private sector's interest in increasing export activity. Citing these demands, the IESC Country Director in Guatemala is confident that more IESC projects will result from increased promotion of IESC's proven ability to deliver both high quality technical assistance and expanded trade and investment services. Concentration in private enterprise will continue to be in the areas of agribusiness, with special emphasis in product development, quality control, and compliance with FDA and USDA regulations; garment or apparel manufacturing; and education and training.

BELIZE

Private Enterprise Environment

Private sector growth is encouraged by the government which welcomes proposals for projects with developmental content; transfers of technology, financial resources or expertise; utilization of natural resources; generation of foreign exchange earnings or savings; and the hiring and training of local employees. Investors are eligible for development concessions which are available for up to fifteen years.

Opportunities for IESC Projects

The two major areas of IESC assistance in Belize are agribusiness and tourism.

Agribusiness

There is little local experience a new agribusiness company can draw from, thus outside expertise is required. Also because of the small domestic market, new companies must, almost from the start, attempt to export. Therefore, although the regulatory and political climate is favorable, business growth in Belize remains difficult. IESC attempts to assist new or expanding businesses will involve helping firms deal simultaneously with financing issues, the constrained domestic market, the need to identify foreign markets, and to cope with the inadequate infrastructure.

Tourism

As an industry, tourism does not have a long history in Belize. IESC volunteers report that export assistance and advice is valued and well-received. Considerable assistance is and will be needed to help manage the growth of the industry and deliver a quality product while protecting Belize's main attraction - the natural environment.

COSTA RICA

Private Enterprise Environment

The private sector is expanding and export of non-traditional products is growing faster than traditional products. CINDE (funded by AID to promote coventures, investments, and export of non-traditional products) and other international organizations continue to provide services to help improve the competitiveness of local private sector firms. The government of Costa Rica offers extensive incentives for investors and is in the process of reducing import tariffs. Its objective is to open the door to increased competition.

Opportunities for IESC Projects

IESC is working closely with CINDE in the following areas: metalworking, plastics, electronics and textiles. These sectors were chosen by CINDE in 1989 as having the greatest potential for the growth of exports. IESC will continue to play a role in evaluating the strengths and weaknesses of selected companies in each sector, and further, to evaluate the training and manpower development needs of these companies. IESC will continue to conduct seminars in these sectors.

JAMAICA

Private Enterprise Environment

The climate for private enterprise in Jamaica has become more favorable in the last twelve months than in the past four years. Privatization and the reduction of government controls and regulations are being implemented in order to conserve hard currency. There is also a willingness on the part of the government to enhance production. Unfortunately, production is mistakenly identified as the answer to earning hard currency, whereas the marketing junction is non-existent. The maturation of the privatization thrust will only thus occur when effective marketing of productive capabilities is accomplished.

Opportunities for IESC Projects

This brings about an incredibly good opportunity to engage the many facets of IESC expertise. Marketing, sales, product design, packaging, advertising, warehousing, distribution, finance - all phases of effective techniques to produce goods and services that can be marketed as potential projects for IESC. The IESC Country Director in Jamaica estimates a growth rate of double the present project starts over the next two to three years.

EL SALVADOR

Private Enterprise Environment

There is a general acceptance of the new government's intention to pursue economic reform policies. The attitude of the private sector in El Salvador is positive. Many express what seems to be a national resolve to recover the losses caused by the last ten years of civil war. Salvadorians also express their willingness to work hard to regain their former influential role in the economy of Central America.

Negatively affecting Salvador's private enterprise environment are the credit limitations imposed on businesses attempting to expand or simply maintain operations. These limitations are the result of banks' lack of liquidity.

Many Salvadorian businessmen state that U.S. investors are not as aggressive as those from other countries, e.g. Germany Taiwan, Spain, Japan, Mexico. And because U.S. companies are so poorly represented, Salvadorians have found that U.S. technology is not their only alternative as they consider improving or beginning new operations.

Opportunities for IESC Projects

A trade and investment program has been started that will both showcase IESC's abilities and help strengthen private enterprise activity. IESC also will work with a national organization in the privatization of the National Agricultural School. Other opportunities in which IESC will be able to assist the private enterprise sector are the privatization of banking system; education, and continued direct assistance to small and medium businesses.

HAITI

Private Enterprise Environment

The private sector in Haiti is experiencing a period of turbulent transition. Because of the new regime, the private sector must adapt not only to new rules concerning customs and taxes, but also currency devaluation, domination of the economy by a limited number of major industrialists, increased union activity , and on-going corruption. On the other hand, there have been some changes which have brought about a certain economic liberalization. Some parts of the private sector see opportunities in the otherwise bleak economic situation in the form of import substitution, while others see greater opportunities in both traditional and non-traditional exports. The major problem for these companies continues to be the difficulty of competing on a global basis.

Opportunities for IESC Projects

It is precisely because the government has not provided the necessary structures to support private enterprise that IESC can be so effective. It is because of global competition that the private sector needs IESC Volunteers. It is because the private sector represents the most effective earner of much needed foreign exchange, the greatest source of productive employment and the most efficient provider of goods and services that IESC Volunteers are so important.

IESC expects to assist specifically in the areas of agro-industry, export marketing, manufacturing for export (both traditional and non-traditional industries), and general management and operational improvement.

EASTERN CARIBBEAN

Private Enterprise Environment

The economies of the islands are being reasonably managed and foreign investment is welcomed while attractive incentives are offered. In Barbados, the government has developed incentives and support services to attract investments. These include tax holidays, low cost factory space and duty-free treatment for project imports. Currently, the best prospect areas for investment in Barbados include food processing, data processing and manufacture of pharmaceuticals and medical equipment.

The governments of St. Lucia, Grenada, Dominica, St. Vincent and the Grenadines actively encourage private foreign investment which they see as a major contributor to development. The U.S. government-funded High Impact Agricultural Marketing Program (HIAMP) offers venture capital for non-traditional, export-oriented investments in agribusiness and fisheries in the Eastern Caribbean.

Opportunities for IESC Projects

In the Caribbean area, because foreign funding is being reduced, a vacuum is being created, and increased assistance is needed to strengthen local industry which will, in turn, strengthen the economy. In the case of Barbados, the government recognizes the increased need for foreign exchange to replace reduced foreign funding. IESC offices in the Caribbean presently have two USAID-funded local agency contracts that should provide ample funding for the "one-on-one" assistance IESC offers. The first is directed towards agriculture, and should support twenty-five projects. The second contract will support thirteen projects, and like the first, offers traditional technical assistance and group technology transfer training programs in diverse industries.

DOMINICAN REPUBLIC

Private Enterprise Environment

The failure of state-owned corporations has become more evident in the Dominican Republic. Slowly, the government monopoly is being eroded through new legislation that allows free zones independence from the government, resort areas and industrial parks. The state-owned sugar industry, and all the urban and rural water services are equally poor performers. On the other hand, the hotel industry, and tourism in general, has had steady growth and success for several years. All this activity is privately operated. Like industrial production, tourism has been growing notwithstanding the non-existent infrastructure that the state should provide (power, water, good roads).

Opportunities for IESC Projects

IESC believes it can play a substantial role in addressing deficiencies in technology and management skills that the educational system of the Dominican Republic has not been able to adequately provide. As private industry becomes better developed, IESC's Trade and Investment Services (TIS) can be more fully utilized. As a result of the two-year pilot program, TIS assistance in helping link U.S. and Dominican firms was recognized as a valuable service for Dominican firms capable of seeking new partners and new markets.

HONDURAS

Private Enterprise Environment

Honduras has just elected a new government with new ideas for resolving the country's economic problems. Most of the measures this government will propose and install will be strict. However, it is hoped they will lead to a stable and growing economy in Honduras. If these measures succeed, the prospects are good for a market-oriented economy.

Opportunities for IESC Projects

The IESC office in Honduras is working with other development oriented private volunteer organizations in Honduras. IESC's program is directed towards small business and micro enterprises in all areas.

MEXICO

Private Enterprise Environment

Mexico is undergoing major transformation under a new government which is shifting its policy relative to the private sector. The emphasis has shifted to global competition, increasing exports of manufactured goods, developing new tourist sites, and decreasing reliance on oil as a source of foreign currency. In order to reach a competitive position, the government is lowering import tariffs, reducing taxes, and cutting red tape. In addition, the government is selling hundreds of government-owned companies, thereby encouraging private sector investment in these companies.

Opportunities for IESC Projects

The push for privatization and export has created a climate favorable to IESC. Companies are seeking modern equipment, cost control procedures, new marketing techniques, and improvement in quality control systems. The best prospects for IESC projects in the private sector are those companies seeking export markets and are in the process of buying new equipment.

SOUTH AMERICA

ECUADOR

Private Enterprise Environment

Private enterprise in Ecuador is very active, particularly in Guayaquil province. Government restrictions do not hinder local businesses. There are no restrictions on exchange of currency. In general, the commercial activities in Ecuador welcome foreign investment and joint ventures are encouraged.

Opportunities for IESC Projects

Opportunities for IESC projects in Ecuador have decreased since 1987. The exchange rate of Sucres to U.S. dollars was much lower than in 1987, and IESC services were eagerly sought. It is difficult for some small businesses to meet current IESC dollar costs. Direct local AID support will end June, 1990. Thereafter, local AID assistance will be channeled via ANDE, the National Businessmen's Association. ANDE will receive local AID grants which will include funds to cover projects of one to three months.

BRAZIL

Private Enterprise Environment

The newly elected government in Brazil is planning to commit itself to privatize approximately three hundred major state-controlled companies that dominate large parts of the Brazilian economy. Advisors to the new president are free market-oriented and, to the extent that it is politically feasible, they intend to let the market correct as many of the gross inefficiencies as possible in the public sector.

Opportunities for IESC Projects

In the area of privatization, IESC has already benefited from two small milling projects now nearing completion. As IESC's success in privatization projects becomes better known, requests should increase for the kinds of assistance that will help restructure operations, transfer technology, and know-how to privatized companies.

VENEZUELA

Private Enterprise Environment

Since the devaluation of the Bolivar, Venezuela has changed its priorities relative to economic growth. The Venezuelan government has now identified the export of non-traditional products as the number one priority.

Opportunities for IESC Projects

If exporting non-traditional products is to be Venezuela's number one priority, it will be necessary for small and medium-sized businesses to acquire new technology if they are to compete internationally. This fact presents IESC with a significant opportunity for developing new projects.

COLOMBIA

Private Enterprise Environment

One example of the effort to privatize government services in Colombia concerns garbage collection. Approximately 1/2 to 2/3 of garbage collection in the city of Bogota was recently turned over to the private sector. The public unanimously praised the significant improvement in services that resulted. Further privatization of government services is under discussion.

Opportunities for IESC Projects

IESC will continue to support privatization of Colombia's diverse industries through its "one on one" technical assistance program by experienced volunteers.

BOLIVIA

Private Enterprise Environment

During the last five years, the Bolivian economy has begun to stabilize and efforts have been made for economic reactivation through support of private enterprise and liberalized policies. The private sector is lobbying for quick approval of a new investment law advantageous to private entrepreneurs. Many international organizations are also assisting with a variety of programs to promote and improve production. Several bi-national chambers of commerce have been sponsoring seminars and inviting foreign investors to assess the possibilities in Bolivia. At the moment, the atmosphere is positive, but still in the early stages of development.

Opportunities for IESC Projects

The two major industries in Bolivia are petroleum and mining. Many of the companies in these categories are quite small, usually employing less than thirty people. Although Bolivia is of the poorest countries in Latin America, its natural resources in minerals and potential agribusiness are significant. Bolivia is realizing its potential for expansion and need expertise assistance, especially in the area of exporting. IESC expects to continue to assist Bolivia's efforts to maximize its economic potential.

CHILE

Private Enterprise Environment

Last year, Chile elected a democratic government after sixteen years of military rule. There is cautious optimism about economic/business activity in 1990. Private enterprises will be directly affected by major changes such as tax increases and modification to labor laws. The Chilean economy is expected to continue an uninterrupted pattern of growth - but at a lower rate of increase. This economic growth stems for the export boom and the high level of new investments. The export sector has been strengthened by continuing product diversification as well as steady increases in market share in Asia, Europe and North America. These increases have enabled the private sector to access world-wide technology.

Opportunities for IESC Projects

There are many opportunities for IESC projects in the private sector as a result of economic expansion. But, despite the fact that IESC expertise is needed and wanted by small and medium-sized Chilean firms, ninety percent of these firms cannot afford the cost of an IESC project.

PARAGUAY

Private Enterprise Environment

More than a year ago, with a new government in place, Paraguay entered a new era - one leading to democracy and a free-market philosophy. Local currency has strengthened, and the implementation of more favorable foreign investment laws now offer a number of incentives to both domestic and foreign investors. That the climate for investment has improved is evidenced by the confidence displayed by local industry to upgrade and enlarge existing facilities.

Opportunities for IESC Projects

IESC has a product, that, over time, will be very marketable in Paraguay. IESC is now developing promotional material to publicize the benefits of IESC technical assistance to potential clients. It is expected that completion of the Paraguayan projects currently being recruited will generate more private sector interest in IESC assistance.

URUGUAY

Private Enterprise Environment

The change in government resulted in fiscal adjustment and strengthened the private sector. Economic prospects in Uruguay are optimistic. The sale of gold reserves will lower the interest on external debt. In 1989, the budget deficit and high employment resulted in high inflation. However, new laws have been enacted to encourage exports, improve quality Uruguayan products and to privatize government monopolies. It is hoped these actions will result in a zero deficit.

Opportunities for IESC Projects

IESC Uruguay aggressively markets IESC technical assistance projects. It also promotes IESC's ABLE research service to facilitate joint and cooperative ventures between local and U.S. firms. It is expected that, in 1990, the majority of IESC assistance will involve exports. The Chamber of Commerce and Industry, and the Union of Exporters support IESC in Uruguay.

PERU

Private Enterprise Environment

It is anticipated that after the 1990 election, Peru will have a change in government because, in the opinion of many Peruvians, the present administration has ruled for five years without a clear plan, has ignored foreign debt obligations, has liberalized imports with subsidized dollars, and has constrained exporters by controlling their dollar incomes through negative exchange rates. All of this, it is reported, has not only adversely affected export development, but has depressed local consumption as well - multiplying the negative effects of industry and commerce.

Opportunities for IESC Projects

Despite the many economic problems, 1989 was a record year for IESC projects in Peru. There remains a hardcore group of private businessmen who are determined to take advantage of world markets such as the U.S., Asia, and the ECM. Several business sectors (fishing, textiles, food processing, and mining) are aware that IESC can provide considerable assistance as they try to move abroad.

ARGENTINA

Private Enterprise Environment

Argentina is at a threshold of a changing economic environment. The concepts of privatization, market forces, and other free enterprise notions are in vogue for the first time in the last sixty years. The assessment of the IESC Country Director is that this is the result of the collapse of the existing "State Controlled Centralized System", and not out of conviction. Secondly, the private sector has grown dependent on government subsides, handouts, soft-loans which are never repaid, and fixed prices. Subsequently, the changeover to a market economy is going to be very difficult for them.

Opportunities for IESC Projects

Never before have private businesses been in a greater need for IESC-related help. Market oriented management is an unknown science to Argentina and IESC has a unique opportunity to offer its expertise in that area.

FAR EAST

INDIA

Private Enterprise Environment

The environment for private enterprise has improved considerably during the last decade. Industrial policies have been liberalized and the private sector has greater freedom to establish industries, even in areas which were earlier reserved for the public sector. The private sector is being encouraged to diversify, improve the quality of its products and become globally competitive.

Opportunities for IESC Projects

In the past IESC in India has assisted in upgrading technology, improving productivity and conserving energy in approximately sixty private enterprises across the country. Based on past experience, IESC plans to play a significant and growing role in assisting small and medium size enterprises which do not have easy access to new technology such as the automotive industry, agro-processing, health care, capital markets and computer services.

INDONESIA

Private Enterprise Environment

Indonesia has gone from a commodity-dependent nation to an innovative, free market-oriented economy with emphasis on non-oil exports. Foreign investment last year reached the largest amount ever in one single year. New reform and continued clarification of deregulations should fuel the diversification and modernization of the economy. Dozens of new banks have been opened due to deregulation, and the Jakarta Stock Exchange has registered an impressive performance.

Opportunities for IESC Projects

As new businesses start up and older businesses grow, there is more need for IESC assistance in all areas of private sector business. IESC expects help trade associations strengthen their operations with technical assistance to their management and staffs. IESC is also looking forward to an aggressive trade and investment program that is industry and trade association oriented, overlaying technical assistance to individual private sector companies in such areas as shrimp processing, furniture making, handicrafts, tourism and agribusiness.

PAKISTAN

Private Enterprise Environment

The Pakistani government has recognized the country's inadequate infrastructure and is contemplating privatizing oil refining and power generation. The government has already taken steps towards increased privatization by reducing the number of economic sectors closed to private enterprise. Additionally to support growth in the private sector, the level of investment requiring government approval was raised, and the requirements for obtaining bank loans were eased.

Opportunities for IESC Projects

Although the 1990 IESC program in Pakistan will mostly support those clients capable of paying a substantial fee, 1991 appears to be the first year IESC will have a more balanced program, assisting all sections of the economy. In 1991, IESC expects to receive more U.S. government support for work with small private enterprises, a group neglected in the past.

PHILIPPINES

Private Enterprise Environment

There is expansion of activities in both the exports and domestic markets due to the Philippine government's drive for self-sufficiency. In the private sector, there is increased activity in manufacturing. It is expected that expanded activities in the service industry will follow with regards to privatization of state-owned enterprises. Although one government agency is responsible for most projects, some multinational financial institutions are involved with large-scale privatization projects.

Opportunities for IESC Projects

As a result of an increase in activities in manufacturing and service industries, IESC projects will assist primarily in these areas. However, financial constraints limit assistance to those small and micro enterprises that can afford IESC project costs. The other constraint for IESC is the strong presence of other not-for-profit organizations, mostly foreign-based or foreign-funded, which are active in similar markets.

SRI LANKA

Private Enterprise Environment

The government in Sri Lanka is firmly committed to encouraging private sector participation in the country's economy. Several areas reserved for the public sector, such as insurance, public transportation, and hospitals have been opened to competition from the private sector. The government has begun privatization by selecting capable private sector businessmen to manage government-owned industrial companies.

Opportunities for IESC Projects

A real need for continued IESC assistance exists in the areas of technology transfer and management skills. Many Sri Lankan enterprises are currently closely controlled, entrepreneurially managed systems, but they are developing decentralized control through management training. IESC's type of "one on one" expertise is required and will be utilized.

The government has highlighted the need for fast maturing micro industry and slightly larger projects to create self-employment. This will help solve current unemployment problems among youth in Sri Lanka. IESC sees an opportunity for rural farmers to cooperate with existing private sector organizations to provide investment in and management of rural projects. This could also provide an opportunity for self-employment of rural youth.

THAILAND

Private Enterprise Environment

The outlook is highly favorable for growth in Thailand's private sector. The country has become a prime location for export-oriented private investment, contributing significantly to Thailand's economic growth rate. The Thai government is firmly committed to private enterprise, and in recent years has taken more positive steps to encourage private investment, including: provisions of tax concessions and other incentives to industrial projects which are export-oriented, resource-based, labor-intensive, and located outside of the Greater Bangkok Region. The government is also committed to the privatization of government enterprises, specifically in electrification, port management, and related infrastructure projects.

Opportunities for IESC Projects

Thailand is rapidly moving from an early industrial to an advanced industrial country. There is a strong demand for technology transfer in major sectors of the economy. IESC will have opportunities to assist private enterprises in the areas of agribusiness, metals, engineering, plastics and chemicals, light industries in general, and tourism.

BANGLADESH

Private Enterprise Environment

There has been an effort by the government in Bangladesh to improve the private enterprise environment. The government decided to decentralize some of the public sector industries, and financial institutions. Conventional steps were taken to encourage private sector investment in trade and industry. However, for a number of reasons, favorable results from government efforts have not materialized, and private investment in industries has declined. The various reasons include: a breakdown in law and order; general malaise in the society; labor unrest; institutional constraints and a continual decline in the value of local currency. Given the above uncertain business environment, it is understandable that private investors remain shy, and that the private sector, in general, will confine its activities to short-term trading instead of investments in fixed assets.

Opportunities for IESC Projects

There are many good prospects for IESC assistance. Considering Bangladeshi firms' low technological and resource base, almost every private enterprise is a prospective client. Many enterprises are owned and managed as family concerns. For these kinds of potential clients, IESC could introduce modern, professional management techniques into their systems. Other potential clients are likely to be entrepreneurs who have invested in fixed assets for manufacturing a product, but now find themselves unable to break even. A third category of clients is likely to be new investors. These are clients who may require information on planning, technology, manufacturing processes, selection of machinery, and training staff.

AFRICA

KENYA

Private Enterprise Environment

Kenya has various agencies, associations, laws and regulations which, in theory, create an ideal environment for private business and new investment by foreign businesses. Investment promotion banks, and various programs financed with foreign aid, provide short-term and long-term loans and equity capital to new or expanding businesses. New banking laws were passed which allow more flexible banking services. The government has announced that all foreign-owned businesses wishing to expatriate their dividends will now have a waiting period of only one year, as opposed to the present two years.

Opportunities for IESC Projects

The IESC Country Director in Kenya assesses that IESC is not only accepted by the business community, but also by government, which is encouraging expansion of IESC services. However, the implementation of some recommendations made by IESC volunteers is hindered by a lack of reliable infrastructure. Raw material supplies, especially imported materials, are in short supply due to complicated rules and regulations, and difficulty with customs officials. Power and telephone outages also constrain productivity. Since these problems exist in most developing countries, they are not deterrent to IESC assistance. Ample opportunities for IESC projects exist in many sectors.

ZIMBABWE

Private Enterprise Environment

The private enterprise environment in Zimbabwe is such that, more and more, businesses are becoming state-owned. Foreign investment is minimal due to high taxation and the mobility to transfer profits out of the country. Zimbabwe, like many African countries, has a high unemployment rate.

Opportunities for IESC Projects

IESC predicts a 25% increase in projects over that of the previous year. Many sectors can benefit from IESC technical assistance and the IESC Country Director in Zimbabwe is optimistic about expanded opportunities. However, much depends on the actions of the government.

ZAMBIA

Private Enterprise Environment

Recent philosophical changes in governmental thinking and planning are opening the doors for private enterprise. The government of Zambia continues to control the vast majority of businesses, including mining and heavy industry. However, systems are being developed for divestiture and increased growth in the private sector. Foreign exchange is, and continues to be, a major problem.

Opportunities for IESC Projects

The strength in Zambia's future lies in the development of a strong private enterprise related to agricultural and light manufacturing. An IESC program dealing with problems in these sectors and with USAID assistance would be of great help with local enterprises. Technical assistance in the areas of food technology, hotel management, and tourism are also untapped sources for projects.

BOTSWANA, SWAZILAND AND LESOTHO

Private Enterprise Environment

The economic environment in Botswana is favorable for private enterprise and foreign investment because of government incentives, training grants, and other laws favoring private enterprise. Because of large local and foreign financial reserves, capital and availability of machinery and equipment are not problems. Although foreign investment is encouraged in Swaziland and Lesotho, greater emphasis is placed on encouraging and supporting local entrepreneurs.

Opportunities for IESC Projects

The local market for IESC in these three countries is small because a very small population is spread over a very large area. Also, local industry is dominated by South African business interests. There are three areas in which IESC can make effective contributions in these countries. The first is to help manufacturing firms which have the immediate possibilities to export. Assistance in export is essential if employment is to increase in the manufacturing sectors. A second is in training local citizens in technical and management skills. The third opportunity is assisting the development of the new, emerging, small and micro private enterprises.

MALAWI

Private Enterprise Environment

The business climate in Malawi is based on free enterprise, with declining parastatal involvement. The subject is bureaucratic intervention in certain areas, sometimes of a discretionary nature. Export and import substitution items are major objectives, as is continued development of the service sector. While competition is an important objective, there is recognition that in a small economy short of capital, a monopoly is unavoidable and even desirable, provided it is regulated.

Opportunities for IESC Projects

The opportunities for IESC involvement are very good. Interest has been shown by all sizes of companies, including large parastatals with divestiture programs.

NEAR EAST

EGYPT

Private Enterprise Environment

The private enterprise environment in Egypt is not developing as rapidly as its proponents desire, but is definitely moving in the right direction. Some positive signs include: public pronouncements by the president encouraging privatization as a way to eliminate inefficiencies in some industries; public sector projects identified as available for sale, and a five-year Egyptian plan calling for reclamation of desert land for agricultural use. Agricultural divestiture may then proceed rapidly. The government is considering the sale of government assets in joint-venture firms, and is seeking private sector firms that are willing to lease excess capacity in state industries.

Opportunities for IESC Projects

IESC is currently involved with a number of innovative projects involving in privatization of state-owned enterprises, tourism, and agriculture especially the reclamation of desert land for agricultural use. These opportunities will utilize both traditional projects and Trade and Investment Services (TIS).

MOROCCO

Private Enterprise Environment

The private enterprise environment in Morocco is favorable. The government has recently published an impressive list of government entities to be privatized in the next two to three years. Governmental restraints on private enterprise involvement by foreign investors have been significantly lessened. Public instruction also has been given that such ventures shall be encouraged at all levels. This has resulted in a stampede of trade delegations, commercial exchanges, etc.

On the negative side, the supply of credit in Morocco is inadequate and most banks loan only to established customers. This perpetuates the situation in which the major commercial enterprises are controlled by an established elite, and discourages the growth of smaller or new firms.

Opportunities for IESC Projects

IESC, through its traditional program, ABLE research studies, and Trade and Investment Services, is actively serving the private sector export activities and developing US-Moroccan investment ties. In the future, IESC hopes to broaden its services to include assistance in all private sector activities, including educational institutions, insurance companies, and other entities serving only the domestic market. Many government owned firms, such as hotels, designated for privatization, are potential recipients of IESC assistance.

JORDAN

Private Enterprise Environment

After years of price stability, the cost of living rose approximately 26% last year. Local currency adjustments have stabilized the inflation rate, which is expected to be 13% in 1990. Government employees have had no general pay rise since 1985. Private sector workers have done better, but these wages still have not kept pace with recent inflation. In the opinion of IESC's Country Director, the outlook for consumer spending, therefore, is bleak. Business confidence remains low and the government is suspicious of the private sector. The private sector, on the other hand, blames government restrictions, customs duties and red tape for most of their problems.

Opportunities for IESC Projects

Jordan needs to export. In 1989, lack of foreign exchange and the need to create new markets motivated the most sophisticated companies to develop new strategies in order to stay in business. IESC could be of great assistance in this area. IESC will continue to provide assistance in job creation, private investment, and import substitution.

YEMEN

Private Enterprise Environment

The North Yemen business environment is intensely entrepreneurial, but there are a limited amount of financially successful businesses that have expanded their endeavors beyond the traditional trading sphere and into a variety of enterprises such as food, pharmaceuticals, agri-industries, and light manufacturing.

Yemen is still basically a country of small and medium-sized businesses. Very little is exported other than relatively small quantities of newly-found oil. There is still an overwhelming reliance on imports. This has led to a severe foreign exchange shortage.

Opportunities for IESC Projects

Other than one large U.S. oil company, there has been little American investment in Yemen. The expected early passage of a progressive new trade and investment law should enhance investment incentives for Americans and boost the level of activity for IESC's Trade and Investment program.

The two Yemens have agreed to unite, effective this coming November. Prior to that time, some activities will be combined, the two national airlines will be first. The new combined population of 12-13 million will make Yemen the largest country on the Arabian Peninsula. This should provide IESC with even greater project opportunities.

TURKEY

Private Enterprise Environment

The IESC Country Director in Turkey has assessed the private enterprise environment as excellent. The government has privatized its minority holding in several private companies. Coupled with that, the adopted measures which allow freer movement of foreign exchange in export, banking, and other transactions, as well as recent import legislation, has liberalized and simplified movement of foreign goods into Turkey. These developments are important factors in the reshaping of Turkey's economy to maximize private enterprise activity and minimize public intervention.

Opportunities for IESC Projects

The opportunities for IESC projects are somewhat limited to those clients which contribute full costs of the project. This automatically eliminates assistance to small companies. With more financial assistance to the IESC program, the future holds opportunities for IESC in many sectors, as reform takes place. IESC recently initiated a Trade and Investment program in Turkey in which project staff has conducted extensive surveys of local companies and inquiries regarding linkage opportunities are emerging from both U.S. and Turkish firms. This program expects to generate some IESC technical assistance for Turkish firms anxious to export to the EEC in 1992.

Monday, March 19, 1990.

FISCAL YEAR 1990 SUPPLEMENTAL REQUEST: PANAMA, NICARAGUA, AND REFUGEE ASSISTANCE

WITNESSES

BERNARD ARONSON, ASSISTANT SECRETARY OF STATE, BUREAU FOR INTER-AMERICAN AFFAIRS, DEPARTMENT OF STATE

FRED W. SCHIECK, ACTING ASSISTANT ADMINISTRATOR, BUREAU FOR LATIN AMERICA AND THE CARIBBEAN, AGENCY FOR INTERNATIONAL DEVELOPMENT

JAMES H. FALL, DIRECTOR, OFFICE OF DEVELOPING NATIONS FINANCE, DEPARTMENT OF THE TREASURY

PRINCETON LYMAN, DIRECTOR, BUREAU FOR REFUGEE PROGRAMS, DEPARTMENT OF STATE

Chairman's Opening Statement

Mr. Obey. This afternoon the committee will review the Administration's fiscal year 1990 request for $870 million in appropriations for assistance to Nicaragua, Panama and refugee programs.

The Administration's request of $1.6 billion in fiscal year 1990 for callable capital for the World Bank was reviewed with the Secretary of the Treasury in a hearing last week. The administration requested supplementals of $500 million for Panama, $300 million for Nicaragua, and $70 million for refugee admissions. These increases are to be offset by the proposed funding from the Defense and Military Construction appropriations bill check of fiscal year 1990. Based on the Administration's request, we have moved as quickly as possible to hold these hearings today.

I would simply note there is an early warning that we cannot move forward on the appropriation in this subcommittee until all of the issues on Defense Department offsets have been worked out. To my understanding, these certainly have not been as of this moment.

We will start by hearing statements on Panama and Nicaragua, and then move into the refugee request.

Our witnesses today will be Bernard Aronson, Assistant Secretary of State, Bureau for Inter-American Affairs, and Princeton Lyman, Director of the Bureau for Refugee Programs, both of the Department of State; from the Agency for International Development, Mr. Fred W. Schieck, acting Assistant Administrator for the Bureau of Latin America and the Caribbean; for the Department of the Treasury is James Fall, Director of the Office of Developing Nations Finance.

Mr. Aronson.

MR. ARONSON'S OPENING STATEMENT

Mr. **ARONSON**. I apologize. In the last minute I found an error in my prepared statement. They are redoing it. It will be up here in a minute.

Mr. **OBEY**. Just so it was not an error in dollars.

Mr. **ARONSON**. Yes.

Mr. Chairman, first I would like to thank you for scheduling this hearing as quickly as you can and for responding to the President's plea for rapid action as constructively as you can.

About a year ago, as you remember, the leadership of the House and Senate on both sides and the President and Secretary of State signed an agreement in the White House called the Bipartisan Accord on Central America. The reason I bring that up is you were a central figure in making that possible.

It was an extraordinary event for a new administration because we came to you and other leaders of the Congress and asked for your trust and cooperation in trying to end a 10-year divisive debate over this region and try to come together behind a common policy.

To your credit—and we will always remember it—you did trust us, and we worked together. I think that policy has borne fruit beyond anything we would have imagined. Had we not joined together on that basis, we would not see the joy and hope that reigns in Nicaragua today.

I would just like to recall what the President said when he signed the Bipartisan Accord because it is germane to what we are trying to achieve in this supplemental. He said that "I can see a democratic Central America in which all of the nations of the region live in peace with each other, where the citizens of the region are safe from the violence of the state or from the revolutionary guerrillas, where resources not devoted to military defense could be channeled to hospitals, homes and schools. That is a dream of all the people and nations. I hope the Esquipulas Accord and perhaps also the Bipartisan Accord will someday be seen as the first step toward fulfillment."

I think we are on the way toward that fulfillment in Panama, Nicaragua, and I am also hopeful about events in El Salvador. I think we are closer there to starting real negotiations under U.N. auspices than ever before. I am hopeful about the possibilities.

I think what we are doing here, Mr. Chairman, and what we are trying to do together is historically and potentially transforming for this region and for these countries.

In Panama, the process of democracy has already taken root. The process of demilitarization has already begun.

With the elections in Nicaragua, we see the chance for an end of the 10-year civil war, the beginning of a genuine democratic regime, the reduction of militaries on both sides.

We hope that the same bipartisan cooperation that allowed us to get this far will also prevail in the next few steps. We know we have put a large package on your plate, and we know that congressional committees don't like to be rushed.

I would stress one point. We are not asking you and the Congress to move this quickly because we are trying to override committee prerogatives or slip something by you or around you, but only because there is an urgency on the ground.

We are trying to respond to it in a responsible way. I think in both Panama and Nicaragua there is now a revolution of rising expectations brought on by democracy and a chance for economic opportunity that the citizens of those countries haven't felt for many years. That is why we hope that this supplemental can move on the President's timetable by April 5.

ECONOMIC NEEDS OF PANAMA

The economic needs of the two countries are different, and the two components of the package are different as a result. Panama has been subjected to a regime that went on a 20-year looting spree. Everything that wasn't nailed down was stolen. In the final year or two, the regime would write checks on the Central Bank and put them out for circulation; none had assets behind them.

There are now about $1 billion in such bad checks out in Panama. The economic infrastructure, the physical infrastructure, the services of government were exploited and leached and bled to make a small handful of people rich. Now this new government has to try to rebuild and meet rising needs and rising hopes for jobs.

On the other hand, Panama has an economic base that is strong and can be revitalized. This is not an undeveloped country. This is a country that used to have a growing economy.

The principal purpose of this $500 million package, the elements of which I will describe briefly, is essentially to jump-start this economy, to infuse liquidity, capital and credit and investment and jobs back into the private sector primarily to allow it to revitalize and become self-sufficient again.

We don't think Panama in the long term ought to be dependent on the U.S. or any other country as an economic base. We need to do enough and do it quickly enough to help it get on its feet.

Nicaragua enjoys the democracy that its people fought for in 1979. After 10 years of civil war and Sandinista management, the country and the economy are exhausted. Per capita income is back to what it was 50 years ago.

If you asked what was the poorest country in the Western Hemisphere, everybody used to say without hesitation Haiti. Now you have to look at the numbers and you can make a case that it is Nicaragua. There, I think, we do need a more long-term, sustained commitment to help an economy grow, an economy that does not have the base that Panama does. It is essentially an agricultural economy. An awful lot of the professional class fled during the last 10 years.

There are some immediate, urging needs. Planting season begins in April. The rainy season begins in May. One of the central tasks to make this transition work is to allow for the demobilization of the resistance and their return to productive life and to allow Mrs. Chamorro to go forward on her plans to reduce the military.

In either case, you are going to have a large number of combatants coming back to private life, and they need to have jobs. They need to have fertilizer and feed and tools. A significant portion of the Nicaraguan package permits both of those to happen.

We are not asking the committee, nor do we think the United States alone can help these two countries get on their feet and grow. The first burden is on the governments themselves to enact and carry out sound economic policies.

The Endara government is committed, as is the Chamorro government, to a policy of privatization to strengthening and relying on the private sector, to reducing the state sector. Both governments, with our support, are looking to the international community for additional help.

The President personally raised this with European leaders, with Prime Minister Kaifu of Japan. So have other officials of our government.

I could, if you want, Mr. Chairman, go through these pages briefly and give you the highlights.

We have given out a fact sheet which I think goes through in some depth.

With regard to Panama, there is essentially——

Mr. OBEY. I would appreciate if you would give us the specific numbers and just describe briefly what you intend to do with the money, rather than do a justification for it.

USE OF FUNDS FOR PANAMA

Mr. ARONSON. In Panama, of this 500 million, 185 million is essentially a private sector revitalization effort which will provide credits to various businesses with a heavy emphasis on job creation.

They will be channeled through the private banking system with oversight by the government and by U.S. auditors as well.

We can't predict exactly which industries will benefit. We suspect many of those that were looted will be early requesters.

We think the construction industry, manufacturing, tourism, and agriculture will be early claimants for these funds.

As the funds are returned to the government, they will then be available for long term development which in cooperation with the government we would want to see put forward.

Panama used to be a net exporter of rice, for example. Under deterioration that has gone on in the last several years, Panama has to import rice. The farmers need credits, capital to hire workers. They need to repair machinery.

The rice industry might be one early recipient of those funds.

The second component is 140 million for a fast disbursing policy-based public investment program. This would help the Government of Panama deal with the budget deficit it inherited from the Noriega regime which was estimated at 10.5 percent of GDP in 1989, and allow investments in their infrastructure, such as roads, bridges, hospitals, clinics and the like. This would be a relatively fast disbursing program.

Third, there would be $130 million which would go to contribute to an international support program to help Panama clear its arrears with the international financial institutions.

The Government of Panama itself has already set aside an equivalent sum out of their escrow funds that it intends to use.

The final third, which would essentially clear their arrears, would come from other international donors. The long-term needs of this economy for credit will be met in part by gaining access to World Bank, Inter-American Development Bank, and IMF funding. This process will allow them to do so.

It will also allow them to reach agreement with the IMF, which would lead to a Paris Club rescheduling so they can put their official debt on a more manageable schedule.

Finally, there is $5 million for public sector restructuring. This will go to help the new government get up and function, provide for financial management, administration of justice, environmental protection, resource management.

In that program would be some assistance for the new national police, which they are hoping to professionalize and create as a functioning alternative to the old PDF.

USE OF FUNDS IN NICARAGUA

With regard to Nicaragua, the $300 million is divided up somewhat differently. There is $128 million that essentially will go to restoring the productive capacity of the Nicaraguan economy.

One early and urgent need is to have imports to allow the agricultural sector of farmers to get back in business, buy spare parts, fertilizer, credits, hire workers and get ready for the planting season.

Secondly, they need oil. The economic team which Mrs. Chamorro sent up believes they are going to run out of oil as early as May, in part because the Soviet Union apparently front loaded their entire 1990 oil deliveries and the Sandinistas used it heavily during their campaign.

One way they got 300,000 people to their rallies was by requisitioning every bus, truck and carriage that could move and, at government expense, chartering those people there. What they didn't know is that those people might not vote for them.

Another $47 million will be used to help the Nicaraguan resistance return and resettle peacefully to civic life. We want to turn fighters into farmers.

Those people have been homeless and refugees for many years. We think providing some economic incentive, however modest, would help the demobilization process.

This would provide for their transportation, seeds and tools to help 15,000 combatants and 45,000 family members return.

Another $75 million will go for economic growth and development. This is going to meet a broad spectrum of need, rebuild schools, help clinics, roads, community facilities, provide medical equipment, commodities, training and other support for the health sector, provide some support for the government for policy planning and public management, provide some support for democratic institutions to get on their feet and vie for political power.

There will be money for small farmers and a fair amount for primary school education and vocational education. There is a $50 million component which would allow Nicaragua to begin to clear its arrears with the international financial institutions. In some ways they are in better shape. They don't owe any money to the IMF.

They do have a World Bank and IDB arrearage problem. Other European countries have agreed to this. Again, they need to have access to international financial flows. This would help them in that process.

I think that describes the two packages. Obviously we can go into more detail, Mr. Chairman.

I would like to close and reiterate the point I began with, which is this is not a technical quick fix we are asking for. We honestly believe that Central America and Panama have a chance to transform themselves in a way that those people have dreamed of doing and yearned to do for generations.

That is to create a permanently democratic and permanently peaceful region where resources can go into schools and medicine and jobs and bettering lives for other people, and not into militaries that will no longer be needed either to suppress their own people or to guard against guerrilla uprisings.

I think this package is crucial to realizing that dream. I think we are well on our way.

Thank you, Mr. Chairman.

[The prepared statement of Mr. Aronson follows:]

TESTIMONY OF BERNARD W. ARONSON
ASSISTANT SECRETARY OF STATE
BUREAU OF INTER-AMERICAN AFFAIRS
BEFORE THE
SUBCOMMITTEE ON FOREIGN OPERATIONS
COMMITTEE ON APPROPRIATIONS
U.S. HOUSE OF REPRESENTATIVES

March 19, 1990

Chairman Obey, ladies and gentlemen, I am pleased to have the opportunity to testify today on the Administration's request for a combined supplemental fiscal year 1990 appropriation to assist both Panama and Nicaragua in the difficult task of economic recovery. The two countries have very different needs, but in both cases the need is urgent.

I know you share my elation over the transformation we are seeing from dictatorship to democracy in this hemisphere and indeed around the world. We have worked long and hard to see democracy bloom in these countries. We have devoted extensive resources, both capital and human, to reach this goal.

The voice of democracy has spoken in Panama and Nicaragua. In Panama, the voice was delayed -- but not stilled. In Nicaragua, we can marvel at how a people who have been intimidated for years could line up quietly at polling places and vote for democracy.

But democracy is fragile, particularly in countries ravaged by years of corrupt and inefficient management. In countries such as these, a vote is not enough: we must now support democracy with assistance so the new governments can stabilize their economies, grow, and allow the benefits of that growth to be felt by the population as a whole. There must be assistance over time for the institutions of democracy to strengthen, take hold and flourish.

These are the broad aims of our fiscal year 1990 supplemental request for Panama and Nicaragua. We hope during this and other testimony to explain the program and elicit the support of the Congress. The funds being requested are absolutely necessary to accomplish the objectives cited. In addition, we are working closely with the international donor community and consulting with the international financial institutions to seek a broader package of support.

These countries need and deserve a strong U.S. response, which is commensurate with their need and our foreign policy interests.

PANAMA

I would first like to offer my thanks to the Congress for the rapid action taken in early February to authorize emergency assistance to Panama. The Administration has now concluded agreements with Panama providing over $42 million including disaster relief assistance. This money is being used for the reconstruction of apartments in the Chorillo district of Panama City; helping other residents of Chorillo purchase new housing; contributing to essential short-term employment-intensive public works programs; providing financing for small businesses, many of which suffered from looting in the aftermath of military operations; providing technical assistance and commodities to the Ministry of Health, the Ministry of Public Works, and other agencies; and helping to improve the administration of justice in Panama.

The emergency assistance authorized last month has also opened the door to commerce and investment. All trade benefits denied to the Noriega regime have been restored. Panamanians may now export almost any product to the United States duty-free with the restoration of CBI and GSP benefits. Access to the U.S. market in sugar was reestablished in January, enabling Panama to ship nearly 70,000 tons of sugar worth more than $30 million to the United States between now and September. With the recovery of these benefits and restoration of stability and confidence, we expect Panama's exports to recover to pre-crisis levels. But recovery will depend greatly on whether new investment flows in to enable the private sector to grow and take advantage of these opportunities.

The emergency assistance that we have extended over the past two months has helped Panama avert immediate disaster. But Panama is not out of the woods yet. This has been only the first phase. If the democratic government of Guillermo Endara is to succeed, if the Panamanian economy is to be set on a sound footing, if those conditions that led to the rise of corruption and tyranny under Noriega are to be rooted out of Panamanian society, then we must follow through with assistance in 1990.

Unemployment in Panama's urban areas is running over 30 percent. The Noriega regime's plundering of the country's coffers and two and a half years of economic and political crisis left Panama in a disastrous fiscal state with massive arrears to both domestic and foreign creditors. In an effort to cover their crimes and to ensure the failure of the new government, Noriega henchmen destroyed records and equipment in key ministries. The Endara Administration has been laboring to reconstruct fiscal order and produce a viable budget for 1990. Budget preparation is in its final stages. One thing is clear, though; the Panamanian government by itself cannot achieve the combined goals of meeting current obligations, restoring credibility among its international creditors, and investing for the future.

The second phase of our assistance proposal will go a long way toward helping Panama meet these goals. The first component of this package is $185 million to revitalize the private sector. Panama has traditionally had a thriving and active business community. But years of abuse and poor policies by the Noriega regime led to a severe contraction. By forcing the National Bank of Panama to finance its huge deficits, the regime brought on a crisis of confidence. This led to a run on the bank, and necessitated the freezing of most bank accounts. With the domestic banking system seriously impaired, investment capital was withdrawn from the country, and the economy withered.

Private sector revitalization funding will help restore confidence and unlock the Panamanian financial system. By the very fact that these funds are directed toward the private sector, it is impossible for me to say precisely where they will be used. To a great extent, the market will determine that. I can say, however, that in addition to traditionally strong areas like commerce, there has been renewed interest in construction and tourism, and promising developments in nontraditional manufacturing and agriculture.

We are developing a system of channeling these funds through the Panamanian banking system in a way that will ensure accountability and productive use of the money. Loan applications might be evaluated on the basis of general creditworthiness of the applicant, effective use of the funds, creation of jobs. We anticipate that some of the first applicants will be the victims of the December looting. Loans to help them reestablish damaged commercial enterprises will quickly restore jobs lost in the aftermath of the military action.

The second part of the package, $140 million for a short-term public investment program, will contribute to two critical goals. It will first provide funds for rapid reconstruction of infrastructure badly run down during the Noriega years. But of equal importance, this component will provide a means for encouraging sound reform of economic policy. Without these funds, Panama will have to forgo essential rehabilitation that would form the foundation of the private sector revitalization and at the same time would reach the poorest segments of the population. Significant funds for these purposes are not likely to materialize from any other source this year.

The Endara Administration has already identified several crucial areas where public investment can be used for rehabilitation and expansion. These include clinics, education facilities, roads, bridges, power generation, water systems, and agriculture. Disbursement of these funds will move in tandem with policy reform. The Endara government has acknowledged the need for reform and is taking important steps in this direction. Expenditures have been cut back sharply and collection of revenue has improved. Beyond this, however, we propose to encourage the Panamanians to reach agreement with the IFIs on appropriate fiscal targets and on goals toward privatization of state-owned enterprises.

Third, we have proposed a contribution of $130 million toward clearance of Panama's arrears with the IMF, World Bank, and Inter-American Development Bank. Arrears accumulated during the last years of Noriega's rule as a result of his strategy of diverting government funds to the pockets of his supporters, combined with blatant disregard for Panama's obligations to its creditors. The country's arrears to the international financial institutions are approaching $600 million. Clearing these arrears is a prerequisite for receiving new loans from the international financial institutions, which were Panama's chief source of development financing before the crisis, and should provide substantial funds in the future.

President Endara has already committed his government to matching the U.S. contribution of $130 million, using funds to be made available from blocked accounts in the United States. I am confident that other governments will also contribute significantly toward clearance of Panama's arrears. Ultimately, by clearing its arrears and meeting current payments on debt Panama will be able to regain access to considerable financial resources from the international financial institutions. We also anticipate that in the coming weeks, Panama and the IMF will agree on a shadow program which will in turn enable Panama to reschedule official bilateral debts through the Paris Club.

The final component, $45 million for public sector restructuring and development support, will contribute directly to policy reform. This relatively small part of the package will produce a big payoff in supporting democratic institutions.

Several important uses of these funds are planned. The Endara government has asked for -- and can greatly benefit from -- technical assistance for public financial management, budget planning, privatization, and tariff reform. Building an effective non-political Public Force to supplant Noriega's corrupt Panama Defense Force is another key goal. Funding for improvement of the judicial system, for better court administration, and for police training -- including training in counternarcotics and anti-money laundering -- would also be included in this package.

Some of the $45 million would be available for the continuation of scholarship programs for young Panamanians. We envision another portion for private-sector support, for example in promotion and development of nontraditional products.

Finally, we plan to include assistance in environmental protection and management of natural resources. The watershed of the Panama Canal must be carefully maintained and the tropical rainforest covering most of the country must be preserved to ensure Panama's future wellbeing, as well as our own.

Despite the deep economic crisis, there are signs of hope for Panama. Optimism and resurgence of confidence have contributed to an increase in bank deposits and some new investment. A U.S. private-sector mission led by OPIC President Zeder recently returned from Panama with some excellent investment prospects. The restoration of trade benefits I mentioned earlier hold out additional promise for export growth. Panama's annual trade exposition last month attracted participants from 25 countries and included many U.S firms.

Deep structural problems remain, however, and can be best addressed through the sort of assistance package that the Administration has presented.

NICARAGUA

INTRODUCTION

On February 25, the Nicaraguan people accomplished a remarkable feat, one that, except in Eastern Europe in recent months, had never been done before: they voted out of office a Marxist government. They did this quietly, almost reverently, while suffering the ravages wrought by a government which had led the country to ruin.

The elections pitted two very different world views. Nicaraguans chose to join a growing list of nations worldwide whose people have opted for peace, democracy and an market-oriented economic system.

Mrs. Chamorro's victory validates the bipartisan approach adopted by this Administration and Congress last year. The advent of democracy in Nicaragua brings us very close to the fundamental U.S. vision for Central America: a region which focuses on democracy and development -- rather than Marxism and militarism. Under Mrs. Chamorro, Nicaragua will aim to reduce its army, the largest in Central America. Those who wish to leave the army will have priority in assignment of State-owned land being distributed through the agrarian reform. Those wishing to remain in the cities will be offered vocational training. Funds thus freed by cuts in Nicaragua's military budget will be able to be used for productive purposes.

Mrs. Chamorro's government has a mandate for change. This mandate needs to be joined by rapid, effective action right away, starting on April 26th, to achieve her government's principal goal: the social and economic recovery of the Nicaraguan people.

THE ECONOMIC DEVELOPMENT CHALLENGE

Today, Nicaragua is a virtually bankrupt nation. Over the past six years, the Nicaraguan economy has declined steadily due to the combined effects of economic mismanagement, civil war, the economic embargo and a hurricane. Real GDP per capita has fallen by over 40% since 1980 to just over $300, making Nicaragua one of the poorest countries in the hemisphere. Unemployment has soared to about 30%. Inflation was over 20,000% in 1988 and is estimated to have raged at 1,500% last year.

A significant part of the country's productive capacity is in the hands of the government: 40% of arable land; 60% of industrial production and 70% of transportation is controlled by an inefficient and totally politicized bureaucracy. The Sandinista government has racked up a public external debt of $7.3 billion, about 2.5 times GDP.

These figures are one-dimensional, as are all economic data. Nicaragua is a country where reliable statistics are simply unavailable. In fact, since 1986, publishing unsanctioned economic statistics has actually been a crime.

But the human dimension of the problem is all too visible: virtually no construction is going on in any of Nicaragua's major cities. No houses are being built. Few cinder block houses exist, even in Managua. The majority are wooden shacks thrown up by squatters who have taken over land on the edge of urban areas.

Visible poverty abounds throughout Latin America and the Caribbean. However, in Nicaragua, it is as stark as anywhere in the hemisphere. An officer in our embassy who previously served in India reported that campesinos at UNO rallies in northern Nicaragua were as emaciated as any group of people he had seen in eastern India. The average Nicaraguan eats two meals a day.

THE U.S. RESPONSE

The economic and social situation in Nicaragua is bleak. There is clearly neither time, nor, in light of U.S. budget stringencies, money to waste.

We are moving fast. The Administration has already begun the process of normalizing bilateral economic relations:

o on March 13, the President announced the lifting of the economic sanctions, which removed the trade embargo, o we have begun the steps necessary to restore Nicaragua's sugar quota and to assist the Nicaraguan government to become eligible for preferential treatment under the Caribbean Basin Initiative (CBI) and the Generalized System of Preferences (GSP) and for use of the facilities offered by the Export-Import Bank and the Overseas Private Investment Corporation.

In response to the most urgent aid needs, we have identified a package of $21.15 million in money immediately available which can be programmed without need for legislation or additional appropriation. These funds are to be used for food aid, for repatriation of the Resistance and their families, for health-related assistance, and to support the democratic transition.

The bulk of our assistance package for Nicaragua, however, is the $300 million FY 1990 supplemental request and $200 million we are seeking for FY 1991.

This economic package is designed to mitigate the immediate crisis which will face Mrs. Chamorro on April 26th. I would refer the Committee to the Administration's Fact Sheet on our Nicaraguan aid package which has been distributed for a detailed description of the purposes of the individual elements of the $300 million package.

I simply would like to make several observations about this program.

The FY 1990 package helps Nicaragua to perform four interrelated, critically needed tasks:

- Provide production inputs to catalyze economic recovery;
- Normalize relations with the international financial institutions;
- Repatriate the Resistance and refugees and work toward national reconciliation; and
- Reestablish the foundations for democracy and economic growth.

Production Inputs - $128 million

Agriculture Inputs ($30 million)

Nicaragua's potential is in its agriculture sector. One quarter of GDP, a third of the labor force and two-thirds of export earnings derive from this sector. One of the critical elements of the package, $30 million for agricultural inputs, is designed not only to address the needs of the first planting season under the new government, but also to assist in providing longer-term agricultural commodities, supplies, and equipment. It will be critically important that this first season go well, for both financial and political reasons. Financially, Nicaragua must begin to grow more food to generate the foreign exchange needed to buttress its macroeconomic reform package and provide a means to pay for needed imports.

Politically, we should recall that it was primarily among the urban and rural poor where the UNO coalition garnered most of its support. It is this same constituency that UNO must satisfy it if is to be a success.

Petroleum ($25 million): Private Sector Production Inputs ($73 million)

Nicaragua will need assistance in purchasing required oil and other essential inputs to rebuild its agricultural and manufacturing base. They are concerned that due to front-loading of oil aid from the Soviet Union and Eastern Europe and lack of foreign exchange, Nicaragua may run out of oil two to three weeks after the inauguration.

Mexico and Venezuela had been providing oil at concessional prices, but stopped these shipments when Nicaragua ran up arrears totalling some $700-800 million to these countries. We expect that with some economic recovery underway, Nicaragua's oil needs will be about $80-100 million per year. The funding request here is for three to four months of critical petroleum products.

Inadequate manufacturing equipment, lack of maintenance and spare parts, and diversion of resources into wartime activities have all contributed to a sharp decline in the manufacturing sector: manufacturing production declined by 26% in 1988. U.S. assistance would be made available to reinvigorate the private sector and allow it to import raw materials, equipment, intermediate goods and spare parts.

Normalization of Relations with the International Financial Institutions - $50 million

These funds would be used to assist the Nicaraguan government to clear arrears to the World Bank and Interamerican Development Bank, which are now estimated to total about $234 million. Nicaragua does not have arrears to the International Monetary Fund. We would expect the international financial institutions to be a principal source of development assistance once arrears are cleared and a policy reform package acceptable to these institutions is negotiated. U.S. support would also be linked to development of a sound economic policy framework.

Repatriation and National Reconciliation - $47 million

Voluntary Demobilization and Repatriation of the Resistance ($32 million)

The voluntary demobilization and repatriation of Nicaraguan Resistance fighters and their families is a key element of the Central American Peace Plan, as well as a fundamental objective of the incoming UNO government. To achieve this goal, provisions must be made for returning Resistance fighters to be reintegrated into the Nicaraguan economy. Without economic incentives, the task of convincing Resistance fighters to surrender their arms and return to Nicaragua will be difficult at best. Thus, it is critical that the United States and other international donors provide funds which can be used to support national reconciliation in Nicaragua.

This $32 million request is designed to pay for the costs of demobilizing, repatriating, and reintegrating Resistance fighters into the social, economic, and political life of Nicaragua. These funds will be used to support the demobilization of some 60,000 Resistance forces and family members. The costs of providing transportation, civilian clothes, food, and medicines to demobilized Resistance forces would be covered. The returning Resistance fighters also would be given a basic package of tools, seeds and fertilizers which would permit them to become self-sufficient during the planting season that begins in May. Funds also would be available to provide vocational training for Resistance members interested in returning to the urban work force.

Refugee Programs ($15 million)

Over the past ten years, some 60,000 Nicaraguans have been recognized officially as refugees in neighboring Central American countries and Mexico where they are being assisted by the United Nations High Commissioner for Refugees (UNHCR). Estimates of externally displaced, undocumented Nicaraguans in the region run as high as 535,000. The Central American countries have acted in an exemplary manner in fulfilling their first asylum responsibility to Nicaraguans despite significant economic and social costs. It is not unreasonable for them to expect the U.S. and other concerned nations to assist with safe, voluntary repatriation and initial reintegration expenses which will make repatriation viable. The U.S. Government has been supportive of the Central American peace process, one of whose major tenets is the repatriation of refugees and the displaced, without which regional stability cannot be achieved.

Many of the refugees registered in Honduras and Costa Rica have already indicated that they are willing and even anxious to return to Nicaragua when their security can be guaranteed and vouched for, and they can be reintegrated into Nicaraguan political and economic life. UNHCR is prepared to organize their return and carry out its normal protection functions in Nicaragua to guard against persecution, harassment or discrimination.

Estimates put the repatriation cost at approximately $35 million, which is in line with recent smaller repatriations in the region. A one-year repatriation program would include registration and documentation of the refugees; dispensing of food and personal items for their journey; transportation to reception camps in Nicaragua for medical exams and orientation before travel to their final destinations; and food, construction materials, seeds and farm implements sufficient to sustain rural settlers until their first harvest. We believe that $10 million would be an appropriate U.S. contribution to this endeavor. We have generally provided some 25% of UNHCR'S funding for the region and, given our particular involvement and interest in this instance, a substantial contribution is fully warranted.

We strongly supported last year's International Conference on Central American Refugees (CIREFCA) which, in principle, endorsed $380 million in projects to integrate refugees, repatriates and the displaced. A $5 million contribution from the United States at the upcoming pledging meeting would meet specific urgent needs for reintegration support stemming from the drastically changed Nicaraguan situation and would stimulate other donors to contribute.

Reestablishing the Foundations for Democracy and Economic Growth - $ 75 million

The foregoing three tasks deal principally with Nicaragua's hard economic, financial and commercial needs and with the urgent job of repatriating the Nicaraguan Resistance, their families and Nicaraguan refugees.

This last element of the package deals with creating a firm foundation for self-sustainable economic growth and for consolidating Nicaragua's fragile democracy. Economic stability and growth are not enough; we recognize that it will also be essential that the fruits of that growth be spread equitably throughout the population. At the same time, we need to help the new government meet basic health and education needs, as well as assist in creating a safety net to help the poor and unemployed obtain employment while the economy undergoes the vast reform in store.

The power of the vote is now well understood by all Nicaraguans. What is important from this point on is to help create and strengthen the institutions and understandings which will ensure that democracy is preserved, protected and expanded in that country.

This portion of our assistance -- a total of $75 million -- is aimed at dealing with these requirements. Of this $75 million, we have requested $10 million for an emergency employment program to deal with existing 30% unemployment, to provide the new government some breathing room and the economy some time to adjust. We expect that demobilization of the Resistance and reduction of the Sandinista armed forces will swell the ranks of the unemployed. Important jobs -- not make work -- would be created to repair decaying infrastructure, rehabilitate schools and health clinics and the like.

A medical assistance package of $4 million will respond to critical health needs of all Nicaraguans. A requested $1 million would go to provide additional economic planning and public administration expertise for the government.

The remaining $60 million request is to meet a wide variety of pressing needs:

- $5 million for projects and programs to strengthen democratic institutions, a free press and democratic labor organizations;

- $10 million for additional health care and pharmaceuticals, with particular attention to child survival and maternal health care;

- $15 million would go to the battered but not totally destroyed Nicaraguan private sector. Assistance would be provided to private-sector organizations to provide training, new technology and access to new investment for private entrepreneurs;

- $15 million would go to revitalize the education system. Rapid population growth, resulting in an ever-larger school-age child population, has severely taxed the education system in the country. This assistance would provide needed commodities such as paper, classroom equipment and textbooks.

- $15 million would go to provide needed credit for farmers, as well as additional inputs and assistance with marketing of production.

THE INTERNATIONAL RESPONSE

Our $300 million FY 1990 and $200 million FY 1991 aid package to address the needs of a democratic Nicaragua is substantial. Unfortunately, it is far from adequate. The resources of the international donor community, as well as those of the international financial institutions, will be needed to provide an adequate volume of development assistance to get this economy moving.

Under the Sandinista government, Nicaragua received more than $500 million annually in economic assistance from the Soviet Union and its allies. Support from the West and Japan averaged around $100 million annually in recent years.

Cuba has already indicated that it does not plan to provide assistance to the new Nicaraguan government; sustained support from the Soviet Union and Eastern European countries is questionable.

There are tentative plans to hold donor meetings over the next several months, during which time Nicaragua can state its case and financial needs. We have already assisted the Chamorro transition team in its efforts to garner international support and will continue to work closely with potential donors and the international financial institutions.

CONCLUSION

President Endara and President-elect Chamorro are bold leaders with a clear vision of where they wish to take their countries. While the ultimate objective - the sort of society each seeks - is far off, the journey must begin right away.

They, as I, recognize that there is neither time nor money to waste.

Unfortunately, in the case of Nicaragua, time is really of the essence. We must be sensitive to Mrs. Chamorro's plight. Not only will she shortly be inheriting a failed economy, but the very government which has ruined Nicaragua, and now a lame duck, continues to work against the best interests of the people. We understand that, at least for the moment, the Sandinistas are refusing to cooperate with the Chamorro transition team. Worse yet, it appears that the Sandinistas are threatening to ram a wage increase for public employees through the National Assembly, making macroeconomic management even more difficult after the inauguration. There are also reports of weapons being handed out to militants, and of looting of government resources, as minimal as they are.

We call on the Sandinistas and the UNO government-elect to work together for the humanitarian aim of promoting the economic development and freedom of the Nicaraguan people beginning right now.

Mrs. Chamorro will not have a long honeymoon with the voters. They voted for a change and refused to believe empty Sandinista rhetoric that "Todo Sera Mejor" - "Everything Will

Be Better". All of us -- the Congress, the Administration and the international donor community -- must recognize the need to help Mrs. Chamorro to really deliver on UNO's promises to restore democracy and a decent life for all Nicaraguans.

I urge Congress to act expeditiously in approving this combined supplemental appropriation for Panama and Nicaragua.

Mr. OBEY. Thank you.

MR. SCHIECK'S OPENING STATEMENT

Mr. Schieck.

Mr. SCHIECK. Thank you, Mr. Chairman. I have submitted a written statement for the record. I would like to summarize a few key points.

It is an exciting time to be working in the Latin American Caribbean region. Reality of a free, democratic and stable hemisphere is closer than ever before. As the President has repeatedly stated, "The day of the dictator is over."

We at A.I.D. look forward to working with this subcommittee and the rest of Congress on this important agenda before us.

One important lesson we have learned over the years in our development experience is that each country in which we work has its own set of political, social and economic problems.

These problems require appropriate, and often unique, solutions.

Therefore, even though a country's development can be supported in important ways by programs of regional cooperation, each country needs to be addressed individually.

Although the needs in both Panama and Nicaragua are large, these two countries face quite different problems, requiring different solutions.

Panama is a middle-income country, with a largely urban population. It has a long tradition of broad access to education and health services.

Infant mortality is much lower than in most of Latin America, and literacy is practically universal. The current recession has primarily hurt people in urban areas due to severe unemployment.

Rural areas have been much less affected by U.S. sanctions and looting. The country's fundamental need is a jump start that will restore confidence and get people back to work.

Nicaragua, on the other hand, faces severe economic problems. It was much poorer than Panama when the Sandinista Government took over, and has fallen even further behind Panama and the rest of the hemisphere.

Per capita GDP has fallen almost 50 percent since 1978, and is now around $300—one of the lowest in the hemisphere. Inflation rates have been in excess of 100 percent for the past five years and over 10,000 percent for the past two.

Loss of buying power and consumption has surpassed 70 percent.

Infant mortality and illiteracy are far too high. Bringing them down to an acceptable level such as Panama's level will require a long-term investment. The entire productive structure—far more concentrated in agriculture than in Panama—has been severely damaged.

Recuperation will be slow, and will depend upon successful implementation of a sequence of policy actions by the government: (1) ending the hyperinflation, (2) eliminating a plethora of "command economy" regulations, (3) demobilizing the massive army, (4) encouraging farmers to go back and replant, and finally, (5) finding a way to recreate flexible means for supplying agricultural inputs and increasing access to market opportunities.

The country's economic recovery and achievement of sustainable growth will take five to ten years of commitment and hard work.

Prompt approval of the assistance package is critically important. Though AID has signed agreements to disburse the immediate $42 million package provided to Panama, the second phase of assistance is desperately needed to prevent the loss of private sector confidence in the new government and to encourage International Financial Institutions and third country assistance to Panama.

In Nicaragua, if the new government does not demonstrate economic gains early on, the government will be weakened—to the detriment of democracy in the country and of the Nicaraguan people themselves.

Mr. Chairman, the details of both plans are already before you and the Members of the subcommittee. I have attached a copy of each to my statement to be included in the record.

I will be happy to answer any questions you may have about any specifics or about our overall strategy. Thank you.

[The prepared statement of Mr. Schieck follows:]

PREPARED STATEMENT OF
FREDERICK W. SCHIECK
ACTING ASSISTANT ADMINISTRATOR
BUREAU FOR LATIN AMERICA AND THE CARIBBEAN
AGENCY FOR INTERNATIONAL DEVELOPMENT
BEFORE THE
HOUSE APPROPRIATIONS SUBCOMMITTEE
ON FOREIGN OPERATIONS
MARCH 19, 1990

Mr. Chairman, members of the Subcommittee, thank you for the opportunity to share with you A.I.D.'s perspective on the President's supplemental requests for both Panama and Nicaragua.

Sweeping changes are taking place in our world today. We are particularly thrilled with the events transpiring in our own hemisphere. In Panama, democracy returned where it had suffered under more than two decades of authoritarian rule. And in Nicaragua, free and fair elections mark a critical step toward peace and democracy in a strife-torn country.

It is an exciting time to be working in the Latin American and Caribbean region. The reality of a free, democratic and stable hemisphere is closer than ever before. As the President has repeatedly stated, "the day of the dictator is over." We at A.I.D. look forward to working with this Subcommittee and the rest of Congress on the important agenda before us.

One important lesson that we have learned over the years in our development experience is that each country in which we work has its own set of political, social and economic problems. These problems require appropriate, and often unique, solutions. Therefore, even though a country's development can be supported in important ways by programs of regional cooperation, each country needs to be addressed individually.

Although the needs in both Panama and Nicaragua are large, these two countries face quite different problems, requiring different solutions.

Panama is a middle-income country, with a largely urban population. It has a long tradition of broad access to education and health services. Infant mortality is far lower than most of Latin America, and literacy is close to universal. The current severe recession has primarily hurt people in urban areas due to unemployment. Rural areas have been much less affected by U.S. sanctions and looting. The country's fundamental immediate need is for a "jump start" that will restore confidence and get people back to work.

Over the longer term, the country also needs better economic policies, such as the elimination of numerous monopolies and special privileges, and the improvement in efficiency of delivery of government services. Such policy improvements will make possible more rapid economic growth, with increases in incomes and productive employment.

The Endara Government has committed itself to take the necessary policy actions, and our assistance will be linked to progress in these areas. Economic recovery can be expected within 1-2 years, although some changes -- strengthening democratic processes, improving public administration -- will take longer.

Nicaragua, on the other hand, is an economic basket case. It was much poorer than Panama when the Sandinista Government took over, and has fallen further behind both Panama and the rest of the hemisphere. Per capita GDP has fallen by almost 50 percent since 1978, and is now around $300 -- one of the lowest in the hemisphere. Inflation rates have been in excess of 100 percent for the past five years and over 10,000 percent for the past two. Loss of buying power and comsumption has surpassed 70 percent.

Infant mortality and illiteracy are far too high. Bringing them down to Panama's level will be a long-term task. The entire productive structure -- far more concentrated in agriculture than in Panama -- has been severely damaged.

Recuperation will be slow, and will be dependent on successful implementation of a sequence of policy actions by the government: ending the hyperinflation, eliminating a plethora of "command economy" regulations, demobilizing the massive army, encouraging farmers to go back and replant, and finding a way to recreate flexible means for supplying agricultural inputs and increasing access to market opportunities. The country's economic recovery and achievement of sustainable growth will take 5-10 years of hard work.

For Panama, our strategy is to help the Endara Government stabilize the economy and rebuild a basis for renewed, sustainable growth. The new government has already made real and substantial achievements to date, in part because of the immediate assistance we made available. In order to help Panama continue to consolidate and expand its economic recovery, we believe that a one-time influx of assistance on the magnitude that we have requested is the most prudent course of action. Assuming our program is implemented promptly, we do not foresee a need for continuing, multi-year, substantial aid flows.

Our strategy in Nicaragua is quite different. A full turnaround in the economy is not realistic. The economic reconstruction needed will take several years to accomplish. Once immediate recovery measures take hold, U.S. assistance will be needed to support the new government's efforts to restructure the economy and the public sector, to reinvigorate private initiative and to ensure the benefits of development are widely shared.

In both cases, prompt approval of the assistance package is of critical importance. Even though A.I.D. has signed agreements to disburse the immediate $42 million that was provided to Panama, the second phase of assistance is desparately needed to prevent the loss of private sector confidence in the new government and to encourage IFI and third country assistance to Panama. And in Nicaragua, if the new government does not demonstrate economic gains early on, the government will be weakened -- to the detriment of democratization and the Nicaraguan people. I urge immediate action on the supplemental request.

Mr. Chairman, the details of both plans are already before you and the members of the Subcommittee. I have attached a copy of each to my statement to be included in the record. I will be happy to answer any questions you may have about any specifics or about our overall strategy. Thank you.

3/15/90

FACT SHEET

Nicaragua: A Commitment to Democracy, Reconciliation, and Reconstruction

U.S. assistance for Nicaragua's economic recovery is designed to support the Chamorro Government in its efforts to democratize, demilitarize, and develop the economy. The Administration believes that urgent economic assistance from the U.S. will be essential to achieve these objectives. The government's most urgent needs are to stabilize the economy and initiate reforms necessary to rebuild it. External assistance will be a critical factor, and a sound overall economic policy framework in Nicaragua will be essential to ensure a sustainable recovery effort.

U.S. assistance alone will not address all of Nicaragua's needs. The U.S. plan will be part of a multilateral effort, in which we anticipate other countries and the international financial institutions, particularly the IMF, will play pivotal roles. Food aid, medical supplies and equipment, and agricultural supplies will be critical to meet the basic needs of the poor. Immediate financing will also be critical to alleviate the constraints posed by massive arrears to foreign creditors.

Background

Over the past six years the Nicaraguan economy has declined steadily due to the combined effects of economic mismanagement, civil war, the trade embargo, and a hurricane. Real GDP per capita has fallen by over 40% since 1980 to just over $300 per capita, making Nicaragua one of the poorest countries in the hemisphere. Unemployment has soared to about 30 percent. Imports are three times as large as exports and are being financed mostly through transfers from the Soviet Bloc. Inflation rates were over 20,000 percent in 1988 and were estimated at over 1,500 percent in 1989. A significant part of the productive apparatus is in the hands of the state and absorbs well over 80 percent of new credit oriented to the productive sector. The public external debt of 7.3 billion dollars represents 2.5 times GDP.

The Response

The President has announced a small immediate action program which can be carried out without legislative action. Work has begun to ensure that the benefits of this first assistance package will be available as soon as possible. These limited resources will help begin the process of national reconciliation and support initial movement toward economic recovery.

The President has:

-- Lifted the economic sanctions, which removes the trade embargo.

-- Begun the steps necessary to restore Nicaragua's sugar quota, and to assist GON to become eligible for preferential treatment under the Caribbean Basin Initiative and the Generalized System of Preferences and for use of the facilities offered by Export-Import Bank and the Overseas Private Investment Corporation.

Among the elements of our economic assistance available without legislation are:

-- Funds for the repatriation of the Resistance and their families, and, for medical care under the Survival Assistance from Civilian Victims of Civil Strife in Central America Program ($7.5 million).

-- PL 480 Title II ($3 million) to be used for targeted feeding for nutritionally vulnerable groups; PL 480 Title I ($10 million) Food for Progress to offer urgently needed staple commodities and local currency to help initiate agricultural policy reforms.

-- Funds remaining from the recent election grants, to be used to support the democratic transition ($650,000).

In addition, the President will request Congressional support and prompt action on a budget amendment for an additional $200 million in FY 91 for Nicaragua, consistent with the approach we have taken this year.

The FY 1990 Supplemental funds are sought for assistance to Nicaragua in the following areas:

Restoring the productive capacity of the Nicaraguan economy $128 million

This assistance will be used to support the efforts of the Government of Nicaragua and the private sector to restore the productive capacity of the economy. Such assistance would include funding for:

-- Public and private sector imports of agricultural equipment, spare parts, fertilizer, and other inputs needed to restore the agriculture sector;

-- Petroleum and oil product imports;

-- Private sector imports of raw materials, equipment, intermediate goods and spare parts to rehabilitate existing facilities and stimulate new productive enterprise in the industrial and agricultural sectors.

Repatriation of Resistance and refugees	$47 million

This assistance will be used, directly or through international organizations, to support the demobilization process and to reintegrate Resistance, displaced Nicaraguans and Nicaraguan refugees into the national social, economic, and political life.

Economic growth and development	$75 million

These resources will assist Nicaragua to begin to meet economic growth and development needs, directly or through regional institutions, and may include support for such activities as:

-- Programs to repair, improve, and maintain existing public infrastructure such as schools, health clinics, roads, and community facilities;

-- Provision of medical equipment, commodities, training, and other support for the health sector;

-- Provision of technical assistance and training in economic policy planning and public management;

-- Activities to support the continued development of democratic institutions such as the legislature, courts, electoral institutions, the press, and labor organizations;

-- Provision of technical assistance and training to the private sector to permit the rehabilitation and modernization of private enterprise in Nicaragua;

-- Support for primary school education, university level scholarships and vocational training;

-- Support for the agricultural sector through small farmer credit activities and improvement of input supply and production marketing systems.

Normalizing relations with the international financial institutions	$50 million

To assist the GON to clear arrears to the IBRD and IDB (estimated at about $234 million). These funds would be disbursed as part of a joint multilateral arrears clearing effort. U.S. support would be linked to the establishment of a sound policy framework.

U.S. ASSISTANCE PROGRAM FY 1990 - 1991

OUTLINE

U.S. ECONOMIC ASSISTANCE (FY 90 SUPP)	Estimated $ Amount (millions)	
Restoring the productive capacity of the Nicaraguan economy		128
o Agricultural Inputs	30	
o Petroleum Imports	25	
o Private Sector Imports	73	
Repatriation of Resistance and refugees		47
o Voluntary Demobilization and Repatriation of Resistance	32	
o Refugee Programs	15	
Economic growth and development		75
o Emergency Employment Program	10	
o Medical Assistance Package	4	
o Emergency Economic Policy and Public Management Technical Assistance	1	
o Other Development Assistance	60	
Normalizing relations with the international financial institutions(IFI's)		50
o Arrears to IFI's	50	
TOTAL FY 90 ASSISTANCE		$300
U.S. ECONOMIC ASSISTANCE (FY 91)		
o Balance of Payments	100	
o Development Support	100	200
TOTAL ASSISTANCE PACKAGE		$500

BEGINNING RECOVERY AND RECONSTRUCTION
(FY 1990 - $300 million)

PRODUCTION INPUTS: CATALYST FOR ECONOMIC RECOVERY $128 million

Agricultural Inputs ($30 million). To address the urgent needs of the first planting season, a balance of payments program to finance the importation of seed, fertilizer, agricultural chemicals, spare parts and equipment is essential. Two of the three annual planting periods take place during the remainder of FY90, the "primera" or principal season (May - June) and the "postrera" or secondary season (Aug. - Sept.). Together they represent approximately 80% of the demand for imported fertilizers (approximately 60,000 MT) and improved, hybrid seeds (rice, corn, beans, potatoes and vegetables) all currently in critically short supply. In addition, spare parts, agricultural chemicals and equipment are lacking to initiate the rehabilitation of traditional export crops such as coffee and bananas.

Petroleum Imports ($25 million). One of the greatest challenges in rebuilding the devastated economy will be the supply financing of oil and petroleum products. Nicaragua's import bill for these products which have been supplied mostly by the Soviet Union and Eastern Europe whose continued support is uncertain, was $37 million for the first half of 1989. Early indications from the Nicaraguan Transition Team are that its current supply of crude oil will be exhausted two to three weeks after the inauguration. Therefore, resources will be made immediately available for the importation of three to four months of critical petroleum products. Additional petroleum supplies would be sought from Mexico and Venezuela.

Private Sector Production Imports ($73 million). Foreign exchange will be required for the reactivation of the private sector. Resources will be made available for the importation of raw materials, equipment, intermediate goods and spare parts to rehabilitate existing facilities and stimulate new activities in both the industrial and agricultural sectors. This assistance will support the development of a policy reform agenda and the initiation of reform actions.

REPATRIATION AND NATIONAL RECONCILIATION $47 million

Voluntary Demobilization and Repatriation of Resistance in Honduras ($32 million). These funds would be used to support the demobilization of approximately 60,000 Nicaraguan Resistance members and families back to civilian life ($30M). The Observer Group for Central America (ONUCA), with the consent of the UN Security Council, may have a role to play in supporting the voluntary demobilization and safe conditions in Nicaragua in accord with the Central American Peace Process ($2M).

Refugee Programs ($15 million). The U.S. contribution to refugee activities under UN auspices would be approximately $15M: $10M for approximately 60,000 Nicaraguan Registered Refugees (UNHCR) and $5M for the reintegration of a larger, yet undetermined number of repatriating displaced Nicaraguans (CIREFCA).

REESTABLISHING THE FOUNDATIONS FOR DEMOCRACY AND ECONOMIC GROWTH $75 million

Emergency Employment ($10 million). In the spirit of national reconciliation and to address even higher unemployment levels, now estimated at 27%, as a result of the demobilization of Resistance and reduction of the Sandinista armed forces, an emergency employment program would be initiated. Jobs would be created for activities such as the repair and improvement of existing public infrastructure, rehabilitation of schools and health clinics, renovation of deteriorated community facilities and other identifiable maintenance projects.

Medical Assistance Package ($4 million). Medicines, medical health personnel, equipment, supplies and services would be provided. Medicines and supplies would cover requirements for traumatic injuries, as well as more common treatments for endemic ailments such as severe malnutrition. This package would also respond, in part, to the medical needs of those victimized by years of civil strife in Nicaragua including the Resistance, civilians and the Sandinista Army personnel.

Economic Policy Planning Public Management ($1 million). Immediate access through a grant to a qualified Central American management institution to provide economic planning and public administration expertise to assist the new GON in overall economic policy planning including privatization, public sector management and public/private sector dialogue.

Assistance will be provided in the following area based a sound economic reform plan:

Democratic Initiatives ($5 million). The institutions and processes of democracy are, weak and will require significant strengthening. This will be addressed through assistance to democratic institutions, a free press and democratic labor organizations.

Health Sector ($10 million). The health sector is confronted with an ever-increasing population (with growth in 1988 of 3.4 percent) and a shortage of foreign exchange. These funds will provide medicines, and pharmaceutical supplies and equipment currently in short supply. Particular emphasis will be given to child survival/maternal health programs which focus on nutrition, oral rehydration, and immunization.

Private Sector ($15 million). The Nicaraguan private sector has suffered from ten years of attempts to dismantle it; however a core remains and its reactivation is critical to renewed economic growth. Support will be provided to private sector associations to give private entrepreneurs access to technical expertise, new technology and investment to allow them to rehabilitate and modernize their operations.

Education Sector ($15 million). The rapid population growth, lack of budgetary resources and drain on human resources caused by the civil war have placed an enormous strain on the education system in Nicaragua. Critically needed commodities such as paper, textbooks, library materials and classroom equipment will be provided for primary schools. Scholarships will allow socially and economically disadvantaged young leaders to receive technical training in the U.S. University textbooks will be provided in technical fields, including economics, management and the physical sciences.

Agricultural Sector ($15 million). Agriculture accounts for roughly one-quarter of Nicaragua's GDP and employs more than 40 percent of the labor force. Over the past 10 years, mismanagement, lack of foreign exchange and poor economic policies have battered the agricultural sector. Resources will be used for small farmer credit, improved inputs supply and production marketing systems.

NORMALIZING RELATIONS WITH THE INTERNATIONAL FINANCIAL INSTITUTIONS **$50 million**

Arrears to IFIs ($50 million). These funds would assist the GON to clear arrears to the IBRD and IDB, estimated at about $234 million. They would be disbursed as part of the multilateral effort. The IFIs would be expected to review and redesign lending programs in Nicaragua in order to be able to begin disbursements in a timely fashion once arrears are cleared. US arrears-clearing support would be linked to a sound policy framework supported by the IMF.

FACT SHEET

PANAMA ECONOMIC ASSISTANCE

DESCRIPTION OF THE FY-1990 SUPPLEMENTAL - $500 MILLION

PRIVATE SECTOR REVITALIZATION CREDIT $185 million

o The President's economic assistance proposal would help "jump-start" the Panamanian private sector which is the engine of economic growth and job creation. One of the major results of such growth would be to put thousands of Panamanians back to work at all levels of the economy.

o Urban unemployment is estimated to be 34%. Since mid-1987 output declined sharply in all economic sectors. Over the same period real GDP declined by about 27.5%, according to the GOP.

o Approximately $1.4 billion of saving and time deposits remain subject to withdrawal restrictions. The deposit run in 1987 and 1988 resulted in a shrinkage of both domestic deposits and domestic bank lending. While stabilized, the banking system remains far less liquid than had been customary.

o Panamanian banks are individually working to improve their position in anticipation of a lifting of deposit restrictions, now scheduled to be eliminated effective June 30, 1990. These actions include accumulating cash reserves, negotiating extended terms with major depositors, and bilateral arrangements to refinance portions of loan portfolios. These prudent moves inhibit banks' ability to resume lending.

o A major injection of resources is required to recharge the depressed economy and meet the needs for investment, intermediate goods and working capital so that firms can rehire workers. An indication of the extent of Panama's financial needs is demonstrated by the following facts:

--Domestic investment in 1989 declined to $470 million from over $800 million in previous years.
--Imports declined to $822 million in 1989 from nearly $1 billion in previous years.

o There now are preliminary signs that business activity is picking up, but private sector revitalization requires a combination of factors including sound GOP policies to attract investment and an efficient financial sector and resources to put the Panamanian private sector back in business.

o Credits to the private sector would be policy-based and keyed to financial, regulatory and trade reforms. The activity would aim at economic growth and, thus, employment generation through a sounder financial sector and support for the revived private sector.

o The USG would transfer $185 million as a grant. We currently are discussing with the GOP the mechanics and technical details of how the funds would be lent through the banking system to the private commercial sector.

o One idea under consideration would be distributing the funds through either a consortium of banks or a government institution to the private sector. Money would be lent on commercial terms to the borrower with criteria based on economic efficiency, job creation potential and economic development policy considerations.

o Loan proceeds would return to the central government for other development priorities.

o The GOP is especially sensitive to the needs of Panamanian businesses that were looted. Estimation of losses from looting begin at $200 million.

o Because credits would be extended to business applicants on the basis of economic criteria, we can not predict the sectoral distribution with precision. Currently, we expect that the $185 million would be lent to the following high priority sectors of the economy, but this list is illustrative and amounts actually lent to each sector will undoubtedly diverge somewhat from these preliminary estimates.

--Construction: approximately $45 million for revitalizing construction activity, which was at a standstill during the past years of the economic crisis. Unemployment in this sector was over 90 percent and a dearth of low-income housing exists.

--Manufacturing: approximately $50 million for Panama's important light manufacturing firms. Because of the past two years of economic crisis, firms desperately need to replace plant and equipment and to restock inventories and spare parts.

--Tourism: an estimated $30 million to develop the potential for tourism and related services which could be a major contributor to economic growth.

--Commerce: approximately $35 million targeted for rebuilding the commercial sector which was devastated by looting and two years of economic crisis. This would build on our immediate assistance package for small business rehabilitation which the Congress approved in February.

--Agriculture: about $25 million for revitalizing this important sector, which has been hamstrung by lack of credit availability during the economic crisis. Funds would be available for machinery, seeds, fertilizers and storage facilities.

PUBLIC INVESTMENT PROGRAM $140 MILLION

o Noriega's regime reduced public investment from $211 million in 1987 to only $78 million in 1989. The country's infrastructure is in serious disrepair with crumbling roads and deteriorating ports, neglected schools and hospitals and a continuing critical need for medical supplies in government hospitals.

o Assistance would be nonrecurring, fast disbursing and policy based, meaning that we would insist on sound fiscal policies in return for this investment budget support.

o The program would be administered by the GOP largely through contracts with private firms. This program would generate numerous private sector jobs, thus alleviating unemployment.

o In close consultation with the GOP, we are looking at a number of ideas, but the most pressing needs appear to be in the following areas. Amounts and sectors listed are illustrative only, since the GOP has not made final budget and policy decisions. Flexibility will be essential.

--Health/Sanitation: In recent years, the Noriega regime made no funds available to construct or repair hospitals and clinics serving Panama's urban and rural population. Rural areas and some urban areas have minimal water and sewage systems in desperate need of rehabilitation (approximately $35 million).

--Education: Until recent years Panama had been a leader in Latin America investment in this sector. The new government must now construct schools, rehabilitate existing facilities and fund procurement of books and other supplies (approximately $20 million).

--Agriculture: While the new government dismantles the State monopolies, it also must finance infrastructure in agriculture such as repair and rehabilitation of irrigation systems, rural roads and storage facilities (approximately $20 million).

--Electric Grid: To overcome years of neglect, the country's unreliable power system will need repairs and procurement of spare parts. A refurbished electricity grid is indispensible to sustained economic growth. (approximately $20 million)

--Basic Transportation/Communications: An estimated 70 percent of Panama's highways require substantial repairs. The disrepair of ports and facilities will hamper growth of commerce. For economic growth, the GOP must rehabilitate basic telecommunication systems. (approximately $45 million)

ASSISTANCE IN PANAMA'S CLEARANCE OF ARREARS WITH THE INTERNATIONAL FINANCIAL INSTITUTIONS (IFIS) $130 MILLION

o At the request of the Panamanian authorities, the USG has agreed to lead an effort to form an international support group to help clear Panama's arrears and to provide resources to assist the country's economic adjustment efforts. The aggregate arrears to the three IFIs which were $540 at the end of 1989 would be cleared on a proportional basis in a U.S.-chaired support group.

o $130 million of the supplemental would be a U.S. contribution toward the work of the support group. Panama has agreed to make available $130 million from its blocked accounts. Other friendly donor countries would contribute $130 millions.

o The total of $390 million generated in this process would be complemented in the final stages of the support group's work by a U.S. Treasury bridge loan of approximately $150 million linked to resumed IFI disbursements.

o The arrears clearing process will require several months of close international cooperation with other donor countries and close work with the IFIs.

o A successful outcome would also require the GOP to remain current throughout 1990 on its monthly service costs, averaging over $20 million, on its existing IFI loans.

o With a track record of servicing these costs, the IMF would be prepared to develop a "shadow program" with Panama prior to the clearing of arrears. With such a program, Panama would be able to reschedule its official bilateral debt through the Paris Club, possibly by mid-year.

o Once the arrears are cleared, the way would be open for a resumption of substantial lending from the IFIs.

PUBLIC SECTOR RESTRUCTURING AND DEVELOPMENT $45 MILLION

o Noriega's regime left the public sector in a shambles, riddled with corruption, bloated payrolls and plagued by political cronies throughout the bureaucracy.

o Aid would be provided for public sector reform and restructuring to modernize, privatize and decentralize governmental structures. Our goal is to help the Panamanians establish honest and effective governmental institutions.

o Final allocations among activities would be determined through discussions with the government of Panama as its priorities are firmly established. Some of the priority programs which we are designing are:

--Technical assistance for public financial management, fiscal policy, budget planning, tariff reform, and privatization. ($6 million)

--Administration of justice and democratic initiatives, including building a professional police force; anti-narcotics assistance to the police force; support fo strengthening the judiciary and the courts; legislative training; and electoral tribunal assistance. ($20 millio

--Environmental protection and natural resources managemen assistance, with emphasis on the vital Panama Canal watershed; preservation of the tropical rain forest and diversification of the biosystem. ($10 million)

--U.S. scholarships for disadvantaged Panamanian youth under the Central American Peace Scholarship Program. ($4 million).

--Export and investment promotion project for non-traditional products, including services, where Panama has a comparative advantage. ($5 million).

FY 90 Supplemental

U.S. ASSISTANCE FOR PANAMA*
(Millions of U.S. Dollars)

Private Sector Revitalization Credits (estimated sectoral distribution of funds, actual distribution will depend on commercial viability of loan proposals)		185
Construction	45	
Manufacturing	50	
Tourism	30	
Commerce	35	
Agriculture	25	
Public Sector Investment Program		140
Health/Sanitation	35	
Education	20	
Agriculture	20	
Electric Energy	20	
Basic Transportation/Communication	45	
Assistance in Clearing IFI Arrears		130
Public Sector Restructuring and Development		45
Technical Assistance to Public Sector	6	
Administration of Justice	20	
Environmental Protection	10	
Scholarships for Disadvantaged Youth	4	
Export and Investment Promotion	5	
Total		500

*The distribution of assistance set forth in this table is explained in the foregoing paper. The numbers represents the Administration's best estimate at this time, but final outlays undoubtedly will vary somewhat from these estimates. The Administration needs flexibility to move funds to those program areas where they are needed most.

Mr. OBEY. Thank you very much.

Mr. Fall.

MR. FALL'S OPENING STATEMENT

Mr. FALL. Thank you, Mr. Chairman.

I also have an abbreviated oral statement and would just ask that my written testimony be submitted for the record.

Mr. OBEY. Sure.

Mr. FALL. The President has proposed economic assistance for Panama and Nicaragua. They reflect the differences in the economic circumstances of both economies.

Our strategy in Panama is to get a substantial amount of resources to the country right away to help the economy. Panama is a middle income country that is suffering primarily from severe liquidity crisis.

Panama has the potential for rapid economic recovery if sufficient resources become available.

We do not anticipate engaging in a long-term relief effort in Panama.

We have put focus on the private sector in designing an assistance program for Panama because we believe that the private sector is the engine of growth and the most important employer in the Panamanian economy. With financial help to the private sector, businesses can bring their operations back on line and create the sustainable employment needed to reduce Panama's unemployment problem over the long run.

Nicaragua, by contrast, is one of the poorest countries in the hemisphere. Agriculture accounts for something on the order of 24 percent of the GDP and is the mainstay of the economy.

A third of the labor force is employed in agriculture. Two-thirds of exports earnings are derived from this sector. This contrasts greatly with Panama, where services account for 80 percent of GDP.

The critical task, facing Ms. Chamorro's new government will be to stabilize the economy, control inflation and initiate reforms necessary to rebuild the country. This will be a difficult task that will require strong leadership and a commitment to economic reform.

A new government in Nicaragua must overcome 10 years of devastation caused by economic mismanagement, civil war, the trade embargo and natural disaster.

PANAMANIAN ECONOMY

Let me return briefly to the Panamanian economy. Thus far, the Government of Panama has not been able to ameliorate the unemployment problem.

Pending completion of the budget for 1990, the government has been operating on an austere cash flow basis. Immediate needs have been attended to, but authorities have refrained from initiating new programs or dissipating their small cash balances. We anticipate a budget will be submitted to the Panamanian legislature for approval this week.

In addition to the unemployment problem, the Endara Government inherited a financial situation that if not addressed could jeopardize the country's economic recovery. Arrears to the IMF, World Bank and the IDB total $540 million at the end of 1989. In addition, $265 million falls due to the IFIs this year.

The Endara Government is committed to restoring normal relations with the international financial institutions, including eliminating arrears and keeping current on payments falling due in 1990. The Panamanians believe, and I agree, that normalizing relations with the IFIs is essential to putting Panama on a sound economic and financial track.

Clearing arrears will restore Panama's eligibility for expanded financial resources from these three major international creditors.

In addition to new lending, the restoration of normal relations with the international financial institutions will open the door for Panama to a rescheduling of official debts in the Paris Club and talks with commercial banks on any eventual financial arrangement on commercial debt.

President Endara asked the United States to organize an international support group of friendly donor countries to help Panama clear its arrears to the IMF, the World Bank and the Inter-American Bank so it can become eligible for new lending from these key institutions.

$130 million of fiscal year 1990 supplemental budget request for Panama is for the U.S. participation in the support group.

The Panamanians, in turn, have earmarked $130 million of their funds remaining in the United States from the blocked accounts for their contributions to help clear arrears.

The next step is for the government to complete its 1990 public sector budget. Payments to stay current in the IFIs are expected to come out of the Panamanian government's own budgetary resources. We have been assured that servicing these payments is a high priority with the Endara Government.

An IMF team is in Panama now in anticipation of unveiling the budget. We expect that negotiations will begin between the Government of Panama and the IMF on an economic adjustment program that would serve as the basis for the support group's efforts to mobilize resources.

We have had preliminary discussions with a number of other nations regarding the contributions to the arrears clearing exercise. Our objective is that the $130 million set-aside by the Endara Government and the $130 million foreseen in or supplemental request will be matched by an equal amount in aggregate from Japan, Korea, Taiwan, and the European nations.

The resulting $390 million would in turn be added to bridge loan of $150 million from the U.S. Treasury and linked to resumed disbursements from the IMF and the World Bank to close the $540 million in arrears.

Once Panama's economic program is defined, Treasury will call the first support group meeting. I must admit that much work remains to be done by the IFIs in order to have loans ready to go to their boards in the next six months.

Our goal for Panama is to realize a net positive inflows from the IFIs for 1990. That is, we are optimistic that disbursements in 1990 will exceed the $265 million falling due this year, excluding arrears.

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The President's economic recovery program for Panama recognizes the Endara Government short term budgetary situation and the fact that the resources must be adequate to meet its enormous 1990 financing gap.

A considerable measure of self-help by the Panamanians is needed for the program to succeed. This depends on the commitment of the government to reform and on the private sector's ability and willingness to utilize opportunities effectively.

NICARAGUAN ECONOMY

On Nicaragua, I will devote just a few comments on the macroeconomic context of the recovery program and the issue of arrears.

Economic recovery requires that Nicaragua develop a strategy with three objectives: Stabilizing the economy, implementing across the board structural reforms, and clearing arrears. Arrears to the multi-lateral development banks total $234 million. The new government must work with the IMF to develop appropriate economic policies to lay the ground work for sustainable growth. U.S. assistance should be linked to the implementation of economic policy reforms.

An agreement with the IMF could enable Nicaragua to reschedule debts to the official bilateral creditors. In addition, it would help to restore the confidence in the economy and establish international support and cooperation for its economic recovery effort.

Arrears will be dealt with in the context of an international effort. The effort will be slightly different from what we have undertaken for Panama, because Nicaragua does not have arrears to the IMF.

We have already had preliminary discussions with other countries regarding potential support for Nicaragua.

In addition, we have had preliminary discussions with Mrs. Chamorro's economic team, on their economic plans, relations with the IFIs and the development of arrears strategy.

We believe that a strong contribution by the U.S. will help catalyze international donor support for clearing Nicaragua's arrears to the World Bank and the Inter-American Development Bank. In this regard we are looking to the World Bank to take a major role in resolving the problem of Nicaragua's arrears.

Mr. Chairman, the United States remains committed to nurturing successful democratic institutions in both Panama and Nicaragua. This task requires the commitment of timely and substantial resources to respond flexibly to the economic conditions of those two countries.

Thank you very much.

[The prepared statement of Mr. Fall follows:]

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Prepared Statement of
James H. Fall, III
Director, Office of Developing Nations Finance
before the Subcommittee on Foreign Operations
Committee on Appropriations
U.S. House of Representatives

Mr. Chairman and Members of the Committee:

I appreciate the opportunity to appear before this committee to discuss our efforts to assist the newborn democracies of Panama and Nicaragua.

Congress acted quickly to approve P.L. 101-243 that reopened access to trade preferences, investment opportunities and government credits and provided $42 million in emergency assistance for Panama. I appreciate that effort. Quick approval of the first phase of emergency assistance for Panama has allowed us to begin addressing the homeless problem in El Chorillo, to assist modestly in helping businesses hurt by looting, and to provide initial technical assistance to the government.

However, while this is a good start, further assistance is required. My hope is that we can work together in a spirit of bipartisanship to assure that phase two of the Panama assistance package, along with the assistance requested for Nicaragua, becomes available in time to keep economic conditions in these countries from deteriorating further.

U.S. Objectives in Panama and Nicaragua

The President has proposed economic assistance packages for Panama and Nicaragua that reflect the differences in the economic circumstances of the two countries. As you may know, Deputy Secretary Eagleburger and I went to Panama in early January to assess the economic situation. We met with President Endara and his economic advisors, as well as with representatives of the private sector. Based on those meetings and the follow-up work of an interagency team of U.S. experts, we formulated a strategy which we believe provides the basis for sustainable, long-term economic recovery.

Our strategy is to get an appreciable sum of resources to Panama right away as a sort of "jump-start" for the economy. Panama is a middle income country that is suffering from a severe liquidity crisis in the banking system and a cash-starved public sector. Panama has the potential for rapid economic recovery if sufficient resources become available. We do not anticipate engaging in a long-term relief effort in Panama. We have put the focus on the private sector in designing an assistance program for Panama because we believe the private sector is the most reliable engine of growth and employment in the Panamanian economy. With some bridging financial help, businesses can bring idle operations back on line, creating the sustainable employment needed to reduce Panama's unemployment problem over the long run.

Public sector services also are required to support the reactivation of the economy. After years of neglect, the electric supply, road networks, water system and port services are all in desperate need of repair. Investments in health and education also are needed. U.S. assistance is designed to permit a resumption in investment spending, and to help the Endara Government implement its open-market economic policy. A sound economic policy framework will be the basis for sustainable, private-sector led growth.

Nicaragua, by contrast, is one of the poorest countries in the hemisphere. Nicaragua's per capita GDP is estimated to have fallen by over 40% since 1980 to just over $300. Real GDP decreased by 7% in 1987, 8% in 1988 and an estimated 5% in 1989. Agriculture accounts for 24% of GDP and is the mainstay of the economy. A third of the labor force is employed in agriculture and two-third of export earnings are derived from this sector.

This contrasts greatly with Panama, where services account for 80% of GDP.

For Nicaragua, we contemplate with the initial package proposed by the President, a development assistance effort consisting largely of traditional aid programs that could last several years. The new government's most urgent needs will be to secure seed and fertilizer for the May planting season. It also needs fuel and medicines on an urgent basis.

A critical task of Mrs. Chamorro's new government will be to stabilize the economy, control inflation, and initiate reforms necessary to rebuild it. This will be a difficult task that will require strong leadership and a commitment to economic reform. The new government of Nicaragua must overcome 10 years of devastation caused by economic mismanagement, civil war, the trade embargo, and natural disaster.

While the needs are great, we must pay attention to the absorptive capacity of the Nicaraguan economy and its ability to utilize resources effectively. Drastic public sector restructuring will be required. Last year, the government of Nicaragua's fiscal deficit was 28% of GDP. The Nicaraguan government received average annual external loan disbursements of over $500 million (18% of GDP) during 1984-1988. Even so, total external arrears to all creditors built up at about the same annual rate during this period and stood at about $2.5 billion at end-1988.

Like Panama, Nicaragua has arrears to the international financial institutions (IFIs). At end-1989, arrears to the World Bank and Inter-American Development Bank (IDB) totalled $233 million. Nicaragua does not have arrears to the IMF. However, the new government urgently needs to implement an economic reform program that could be supported by the IMF. It also needs to clear arrears to the multilateral development banks as a prerequisite to obtaining new loans from these institutions.

Update on Panama's Economic and Financial Situation

Let me return briefly to the Panamanian economy. I am optimistic about the ability of the Panamanian economy to recover. At the same time, I believe that $500 million in new resources is needed on an urgent basis.

The government of Panama is facing an immediate and severe employment crunch. Unemployment, estimated at 25%, is a major economic and political problem. In 1987, unemployment was only 12%. Urban unemployment is estimated at 34%.

Thus far, the government of Panama has not been able to ameliorate the unemployment problem. Pending completion of a budget for 1990, the government has been operating on an austere cash flow basis. Immediate needs have been attended to but the authorities have refrained from initiating new programs or dissipating their small cash balances in the absence of democratic budgetary authority. We expect the budget to be submitted to the legislature for approval early this week.

In addition to the unemployment problem, the Endara Government inherited a financial situation that, if not addressed, could jeopardize the country's economic recovery. Arrears to the IMF, World Bank, and IDB totalled $540 million at the end of 1989. In addition, $265 million falls due to the IFIs during 1990. Imports have been depressed by an estimated $500 million during the last two years, resulting in an urgent need to rebuild inventories and replenish capital equipment.

The Endara Government is committed to restoring normal relations with the international financial institutions, including eliminating arrears and keeping current on payments falling due in 1990. The Panamanians believe, and we agree, that normalizing relations with the IFIs is essential to putting Panama on a sound economic and financial track. Clearing arrears will restore Panama's eligibly for expanded financial resources from three major international creditors. In addition to new lending, the restoration of normal relations with the international financial institutions will open the door for Panama to a rescheduling of official debts in the Paris Club and talks with commercial banks on an eventual financing arrangement.

President Endara has asked the United States to organize an international support group of friendly donor countries to help Panama clear its arrears to the IMF, the World Bank, and IDB so that it can become eligible again for new lending from these key institutions. Approximately $130 million of the fiscal 1990 supplemental budget request for Panama is for U.S. participation in the support group.

The Panamanians have earmarked $130 million of their funds remaining in the United States for their contribution to help clear arrears. The next step is for the government to complete its 1990 public sector budget. Payments to stay current with the IFIs are expected to come out of budgetary resources and we have been assured that servicing these payments is a high priority with the Panamanian government. An IMF team is in Panama now in anticipation of the unveiling of the budget. We expect that negotiations will begin between the government of Panama and the IMF on an economic adjustment program that would serve as the basis for the support group's efforts to mobilize resources.

We have had preliminary discussions with a number of other nations regarding contributions to the arrears clearing exercise. Our objective is that the $130 million set aside by the Endara government and the $130 million foreseen in our supplemental request will be matched by an equal amount in aggregate from Japan, Korea, Taiwan and the European nations. The resulting $390 million would in turn be added to a bridge loan of $150 million from the U.S. Treasury and linked to resumed disbursements from the IMF and World Bank to close out the $540 million arrears to the IFIs.

Once Panama's economic program has been defined, Treasury will call the first support group meeting. Much work remains to be done by the IFIs in order to have loans ready to go to their boards in the next six months or so. Our goal is for Panama to realize a net positive inflow from the IFIs for 1990; that is, we are optimistic that disbursements in 1990 will exceed the $265 million falling due in 1990, excluding arrears.

During the past two and a half months we have held numerous discussions with senior management at each of the IFIs about the level and timing of their resumed disbursements. Despite the large arrears to these institutions, we wanted to begin the process of planning the reflow of financial resources to Panama.

Under the Noriega regime payment arrears to the IFIs began accumulating in September 1987 - that is two and a half years ago - as Panama's financial resources were diverted to the PDF and other purposes. Disbursements from the IFIs were terminated soon thereafter.

Two key objectives we and the Panamanian government now have are clearing the arrears and reestablishing a positive balance to the financial flows from the IFIs to Panama. An IMF mission, the second since January, is now in Panama to begin this process. The World Bank will soon be sending its second mission to Panama. These missions will enable the IFIs to begin rebuilding the pipeline of disbursements interrupted more than two years ago.

Once the arrears are cleared and U.S. economic assistance contributes to a rebound of Panama's economic growth, the country will be in a strengthened position to service an expansion in IFI loans. Crucial to a successful achievement of these objectives will be congressional support for the requested $130 million in the supplemental as the U.S. contribution to help clear the arrears.

Status of Blocked Accounts

As of March 13, a total of $256 million had been released to Panama from blocked accounts in the United States. A further

$169.7 million remains in escrowed accounts. Of the remaining funds, $122.6 million is in the Federal Reserve Bank of New York. The Panamanian government has not requested the transfer of these funds to Panama because it intends to use them for its contribution to clear arrears to the IFIs, in conjunction with the Support Group. $45.4 million remains in the so-called "509 accounts," pending resolution of outstanding tax questions between the corporate taxpayers and the Panamanian tax authorities. These accounts are blocked reserve accounts that U.S. companies were entitled to keep on their books or with a commercial bank in lieu of making payments into N.Y. Federal Reserve Account #2.

It is our understanding that the escrowed funds released or to be released to the GOP are incorporated as government revenue in the 1990 budget now being finalized by the Panamanian government. The portion not earmarked for clearing arrears to the IFIs will be used to finance regular budgetary expenditures.

During December-February period, tax collections by the Panamanian government were abnormally low. In light of the chaotic conditions prevailing, the GOP deferred the payment date for 1989 income taxes from January 31 to March 15. Tax revenue collections in December were substantially below the already badly depressed levels of December 1988 and only one-quarter of collections in 1986 and 1987. Collections in January and February were unchanged from depressed collections for the same period in 1988. Part of this may be made good as postponed taxes are collected on a delayed basis. However, the looting losses will carry forward and result in a permanent loss in the tax revenue this year.

In addition, the GOP has attempted to regularize some of its internal payments. At the end of the year the government was essentially a month behind in ordinary salary payments. These were brought up to date based on release of escrowed funds at year end, at a cost of $40-50 million. The Noriega regime, in a last ditch attempt to raise cash, had retained payroll allotments and withholdings from government employees' checks. These covered such things as mortgage payments and social security payments. Some $15.4 million was paid during January and February to bring these accounts up to date as of December 31, 1989. A further $13.6 million was scheduled to be paid at the end of February. $2 million of supplier bills overdue from 1985-1988 were also paid and an additional $8 million in overdue supplier bills is being reviewed for payment.

Description of Economic Recovery Package

The President's economic recovery program for Panama recognizes the Endara Government's short-term budgetary situation and the fact that resources must be provided to help meet an enormous 1990 financing gap. It aims to provide assistance as quickly as possible to priority areas identified by the Endara Government. A considerable measure of self-help by the Panamanians is needed for the program to succeed. This depends on the commitment of the government to economic reform and on the private sector's ability and willingness to utilize opportunities effectively. The program would consist of the following broad components:

oo $185 million - These funds, considered balance of payments support, would be deposited in the banking system for on-lending to the private sector.

oo $140 million - These funds would be provided to the Government of Panama to finance a public investment program to generate employment and domestic demand.

oo $45 million - These funds would be provided to the Government to address areas where policy reforms are needed. Assistance would facilitate judicial reform and the needs of the civilian police force, fiscal management and accountability, privatization of public enterprises, the restoration of public services, private sector export promotion and watershed protection for the Canal.

oo $130 million - These funds would represent a U.S. contribution to clear Panama's arrears to the IMF, IBRD, and IDB so that Panama will be eligible for new lending.

Status of Agreements on Bank Secrecy and Money Laundering

We have been very encouraged by indications that the Endara Government is serious about attacking Panama's money laundering problem, that it recognizes the disturbing extent to which its banks have been used to launder drug proceeds, and that it will consider modifying its existing laws and procedures to facilitate criminal investigations and to provide a mechanism for exchanging law enforcement information with the U.S.

The Panamanians have taken a number of concrete actions to demonstrate their commitment to preventing the use of their banking system by narcotics traffickers and other criminals. For example, in late December, the Endara Government froze over 300 bank accounts suspected of being used for drug money laundering. The Endara Government is now obtaining information about these accounts so that it can be provided to U.S. investigators. In early January, Panama signed an agreement with the U.S. to take measures to combat money laundering. On February 13, 1990, the Endara Cabinet issued Decree No. 41 which requires banks to obtain information from their customers about transactions in currency and/or certain negotiable instruments of more than $10,000.

Just last week, a U.S. team consisting of representatives from the Departments of Treasury, State and Justice, participated in a series of meetings with high-level Panamanian officials in Panama to discuss actions that they have taken, and additional steps they could take, to prevent Panama from again becoming a money laundering center. The U.S. and Panama also are discussing various law enforcement agreements. Because of the sensitive nature of these ongoing discussions and the need for internal discussion of the options in Panama, it was agreed that the specifics would remain confidential.

Nicaragua

I do not intend to go into a full description of the President's program for Nicaragua. The State Department and AID representatives are prepared to describe their programs in detail. I will devote my remarks to the macroeconomic context of the recovery program and to the issue of arrears.

Economic recovery requires that Nicaragua develop a strategy with three objectives: stabilizing the economy, implementing across the board structural reforms, and clearing arrears. Arrears to the Multilateral Development Banks total $233 million and arrears to bilateral creditors total about $1.4 billion.

The new government must work with the IMF to develop appropriate economic policies to lay the groundwork for sustainable growth. U.S. assistance should be linked to the implementation of economic policy reforms. An agreement with the IMF could enable Nicaragua to reschedule debts to official bilateral creditors. In addition, it would help to restore confidence in the economy and establish international support and coordination for its economic recovery effort.

Arrears will be dealt with in the context of an international effort. The effort will be slightly different from what we have undertaken for Panama because Nicaragua does not have arrears to the IMF. We have already had preliminary discussions with other countries regarding potential support for Nicaragua. In addition, we have held preliminary discussions with Mrs. Chamorro's economic team on their economic plans, relations with the IFIs, and the development of an arrears strategy. We believe that a strong contribution by the U.S. will help catalyze international donor support for clearing Nicaragua's arrears to the World Bank and IDB. In this regard, we are looking to the World Bank to take a major role in resolving the problem of Nicaragua's arrears.

Conclusion

The United States remains committed to nurturing successful democratic institutions in both Panama and Nicaragua. This task requires the commitment of timely and substantial resources that respond flexibly to the economic conditions of the two countries. In Panama, our effort will be of a more short-term nature. Nicaragua will require a longer term commitment of development assistance. Both countries expect and deserve significant United States support. The people of these nations have suffered greatly. We must not sell them short. Let us not hesitate to demonstrate our solidarity with their struggles and our dedication to seeing that the people of Panama and Nicaragua reap the benefits of their new democracies.

Mr. OBEY. Thank you.
Mr. Lyman.

MR. LYMAN'S OPENING STATEMENT

Mr. LYMAN. Thank you, Mr. Chairman.

I am pleased to comment on the third component of the Administration's request, the $70 million for the refugee program. You have the written statement for the record. I will just summarize briefly.

These funds are required to finance the increase in the number of refugee admissions established by the President's Determination for fiscal year 1990.

The Department's initial fiscal year 1990 budget request provided for 84,000 refugee admissions. After Congressional consultation last September, the President set the funded admissions ceiling at 111,000—an increase of 27,000.

The Presidential Determination also provides for 14,000 refugees covered by private sector funding.

The $70 million request is required to finance the processing, transportation and initial resettlement costs related to the increase of 27,000 refugee admissions of which 24,000 are Soviet, 2,000 are Amerasian, and 1,000 are African. Specifically, this $70 million supplemental appropriations request includes $38 million to pay for the processing and care and maintenance of refugees in Europe, which are provided to them by several voluntary agencies;

$14 million to finance the transportation costs related to bringing the refugees to this country as well as the transportation-related services provided by the International Organization for Migration; and $10 million to provide reception and placement grants to the American voluntary agencies engaged in the initial resettlement of these refugees in this country.

Last year some 37,000 Soviet refugees came to the United States via Vienna and Rome. They did so because that route was almost the only way for Soviet refugees to apply for admission to the United States.

By late last year, however, it had become clear that liberalization of Soviet emigration practice had virtually eliminated the need for the Vienna/Rome route. Accordingly, it was decided to move to the processing of Soviet refugee applicants in Moscow.

However, over 40,000 Soviets were already in the Vienna/Rome pipeline. It is to this group that much of this supplemental is directed.

Under our current plan we hope to have moved the last Soviet refugees out of Europe by the end of May. I can report today we will move approximately 9,000 people in March, the highest month ever.

To replace the Vienna and Rome processing, we established new mechanisms and capabilities in Moscow and Washington, enabling the U.S. Government to respond more effectively and systematically to an ever increasing rate of refugee applications from groups in the Soviet Union who are of special humanitarian interest to the United States.

These procedures are fully in place and working very well. As a result of this change, there will be substantial savings within the admissions program in fiscal year 1991.

I want to mention briefly the other two increases. We are requesting funding for the increase in the fiscal year 1990 ceiling for admission of Amerasians and their family members from 13,000 to 15,000.

As this program proceeded through 1989, we found that we had the capacity to process and admit a larger number of Amerasians than we had originally projected in the budget.

In Africa, we had for years a processing problem in the Sudan which was finally resolved in mid-1989.

This enabled us to increase the number of African refugees we expect to admit this year from 2,000 to 3,000. These funds would finance their admission.

Over the years, implementation of the U.S. refugee admissions program has relied on a partnership between the U.S. Government, several American voluntary agencies, and the International Organization for Migration.

This year, this partnership has had to respond not only to new opportunities but to challenges of carrying out a program with limited resources and without assurances of U.S. Government reimbursement for those costs we normally cover.

The positive response to this challenge has strengthened the tie between the government and the participating organizations.

I want to call attention to the efforts of the thousands of private American citizens who have worked to make our refugee admissions program what it is today and to thank them again as individuals and as organizations in this public manner for all they have done.

Before closing I want to again stress the need for these funds as soon as possible if we are to avoid a serious disruption in the implementation of the U.S. refugee admissions program.

Given the financial constraints and the extraordinary efforts made by so many of the voluntary organizations to get as far as we have, I ask your support and cooperation in responding to this request on an urgent basis.

[The prepared statement of Mr. Lyman follows:]

STATEMENT
OF
AMBASSADOR PRINCETON N. LYMAN
DIRECTOR, BUREAU FOR REFUGEE PROGRAMS
BEFORE THE
SUBCOMMITTEE ON FOREIGN OPERATIONS, EXPORT FINANCING AND RELATED PROGRAMS

MARCH 19, 1990

Thank you Mr. Chairman. I appreciate this opportunity to discuss the third component of the Administration's FY 1990 request for supplemental appropriations -- that portion which seeks $70 million for the Department's refugee programs.

These funds are required to finance the increase in the number of authorized refugee admissions established by the President's Determination for FY 1990. The Department's initial FY 1990 budget request provided for 84,000 refugee admissions. After Congressional consultation last September, the President set the funded admissions ceiling at 111,000 -- an increase of 27,000. The Presidential Determination also provides for 14,000 refugees covered by private sector funding.

The $70 million request for supplemental funds is required to finance the processing, transportation and initial resettlement costs related to the increase of 27,000 refugee admissions of which 24,000 are Soviet, 2,000 are Amerasian, and 1,000 are African. In addition to the costs directly related to the increase in the numbers of refugees to be admitted, these funds are required to provide for costs associated with the care and maintenance of the expanded caseload of Soviet refugees while in transit in Western Europe on their way to this country.

The largest portion of this request covers the increase in the number of funded Soviet admissions from 16,000 to 40,000 and the increase in care and maintenance costs for the entire caseload. In addition to this, the Jewish voluntary agencies have undertaken to finance from private sources the admission and resettlement costs of 8,000 of the 10,000 private sector numbers which are available for Soviet refugees. Thus, the overall ceiling for Soviet refugees in FY 1990 is 50,000.

Specifically, this $70 million supplemental appropriation request includes an estimated $38 million to pay for the processing and care and maintenance of refugees in Europe which are provided by several American voluntary agencies; some $14 million to finance the transportation costs related to bringing the refugees to this country as well as the transportation related services provided by the International Organization for Migration; and $18 million to provide reception and placements grants to the American voluntary agencies engaged in the initial resettlement of these refugees in this country.

Last fiscal year, about 37,000 Soviet refugees came to the U.S. via Vienna and Rome. At that time the Vienna/Rome route was almost the only way for Soviet refugees to apply for admission to the U.S. and the cost of the care and maintenance for these people in Europe had begun to overwhelm the U.S. refugee admissions program budget. At the same time, however, it had become clear that liberalization of Soviet emigration practice had virtually eliminated the need for the Vienna/Rome route. Accordingly, it was decided to move to the processing of Soviet refugee applicants in Moscow. Nevertheless over 40,000 Soviets were already in the Vienna/Rome pipeleine. It is to this group that much of this supplemental is directed. Under the current plan we hope to have moved the last Soviet refugees from Vienna and Rome to the U.S. by the end of May.

To replace the Vienna and Rome processing, we established new mechanisms and capabilities in Moscow and Washington, enabling the U.S. Government to respond more effectively and systematically to an ever increasing rate of refugee applications from groups in the Soviet Union who are of special humanitarian interest to the U.S. These new procedures are fully in place and operating beyond our expectations of last September. As a result of this change, there will be substantial savings within the admissions program in FY 1991.

I want to mention briefly the increase in the number of admissions under the Orderly Departure Program from Vietnam and from Africa. We are requesting funding for the increase in the FY 1990 ceiling for admission of Amerasians and their family members from 13,000 to 15,000. As this program proceeded through 1989, we found that we had the capacity to process and admit a larger number of Amerasians than we had originally projected in the budget. We increased the admissions level in view of the urgency of reuniting these young people and their families with this country whose heritage they possess. In addition, we note the special legislation regarding Amerasian entry, which calls for priority attention to processing this group.

In Africa, we had for years a processing problem in the Sudan which was finally resolved in mid-1989. This enabled us to increase the number of African refugees we expect to admit this year from 2,000 to 3,000. These funds would finance their admission.

Over the years, implementation of the U.S. refugee admissions program has relied on a partnership between the U.S. Government, several American voluntary agencies, and the International Organization for Migration. This year, this partnership has had to respond not only to new opportunities but to the challenge of carrying out a program with limited resources and without assurances of U.S. government reimbursement. The positive response to this challenge has strengthened the tie between the government and the participating organizations. I want to call attention to the efforts of the thousands of private American citizens who have worked to make our refugee admissions program what it is today and to thank them again as individuals and as organizations in this public manner for all they have done.

Before closing I want to again stress the need for these funds as soon as possible if we are to avoid a serious disruption in the implementation of the U.S. refugee admissions program. Given the financial constraints and the extraordinary efforts made by so many of the voluntary organizations to get as far as we have, I ask your support and cooperation in responding to this request on an urgent basis.

DEFENSE DEPARTMENT OFFSETS

Mr. **Obey**. The President asked Congress to approve his request for $870 million, Mr. Aronson, by April 5th. He indicated in his statement that if he did not get approval by that time, we should simply give him the authority to select the offsets. If that did not happen, he would then simply request a Budget Act waiver—the Gramm-Rudman waiver.

I would like to ask a couple of questions about that, because I have seen a number of stories which indicate that, "The Congress cannot choose which offsets to select."

The problem is that under the Gramm-Rudman design, the Congress has no choice but to accept the spending estimates of a neutral observer. In this case, it is the Congressional Budget Office. For Panama, the $500 million expenditure, which you have on the budget authority side, must be offset in the defense budget, so that we do not exceed the Gramm-Rudman ceiling. The Congressional Budget Office says that on the outlay side, in fact, you only produce $90 million worth of offsets, whereas you need $309 million, leaving a shortfall of $219 million.

My first question is, since this subcommittee does not have the authority to deal with the Defense Department offsets, are you any closer now than you were two weeks ago to having actually identified offsets which will reduce the outlays by the amount that you are required to reduce them by, or is the Administration's intent simply to ignore the outlay side of the budget?

Mr. **Aronson**. Mr. Chairman, I just got off a plane where I was in Latin America. This was not the principal item that I was discussing. But I know that the President instructed the Secretary of Defense and the Head of OMB to look at this issue, because there had been some question about the offsets originally proposed in Panama, and in a very expedited way, to try to resolve it. Where that stands right now, I can't tell you. But I don't think it is this Administration's intention, in any way, to lay that issue on the shelf and forget about it. I think they are trying to resolve it in a good faith way.

I can't tell you how much progress they have made at this point, but I will be glad to get you an answer after this hearing.

Mr. **Obey**. Is there anyone here who can respond to that question?

Mr. **Aronson**. Is there anyone from OMB here?

Mr. **Dube**. I am from the DOD.

Mr. **Obey**. Is there any way we can get a chair up here and bring him up to the table?

Identify yourself.

Mr. **Dube**. I am Paul Dube. I am the Deputy Comptroller for Program Budget. Right now we are engaged in negotiations with the committees to find a set of offsets that is mutually agreeable to each of us. We are confident we will do that within the President's time line. It will require give and take.

Mr. **Obey**. The point I am making does not have anything to do with whether or not the DOD and the Administration can negotiate on where the offsets ought to come from. I understand the Congressional Budget Office has indicated that the Administration's own request is $219 million short of meeting that offset requirement. Do you have numbers that would disagree with that?

Mr. DUBE. I have some data that OMB provided me, I believe, on Friday or Monday. It was Friday actually. It shows the total of the two, the Nicaragua and Panama——

Mr. OBEY. I am talking about Panama alone, though.

Mr. DUBE. Frankly, I don't have the CBO rack-up of the Panama subject only. These purport to be CBO's estimates for the two. There is a $14 million difference between their outlay projections and CBO's.

Mr. OBEY. Those are quite different numbers than we have.

My point is simply this. I do not like these rules. I did not invent them, but I have to live under them. In assessing what we can do, you say there is a $14 million difference. I am trying to bring it down so we can actually understand what we are dealing with.

You say you have no CBO numbers with respect to Panama?

Mr. DUBE. Not that only. Not that Panama supplemental only. I have the two mixed together—Nicaragua and Panama.

Mr. OBEY. Staff tells me if you take Panama and Nicaragua and combine them, the Congressional Budget Office estimates that the Administration has a short fall of $252 million on the outlay side.

Mr. DUBE. I suspect——

Mr. OBEY. Including the refugee total of $47 million.

Mr. DUBE. I suspect there is a difference there. It is probably in scoring the deferrals. Part of the outlay reduction that the Adminsistration felt was offsetting the Panama supplemental was the deferrals that the department has proposed in fiscal year '90. If they are scoring those, and I assume they are——

Mr. OBEY. I am told this does not include the deferral scoring.

Mr. DUBE. If it doesn't, that accounts for the magnitude of the difference between us.

Mr. OBEY. No, that is not my understanding.

Mr. DUBE. I will be very surprised if the difference of that magnitude is related to a difference in the assumed outlay rates.

Mr. OBEY. Here is my problem. This committee is being told by the President, "boys, you got to move." Our problem is that you may have this problem worked out with the Defense numbers by the President's deadline. But if we are to meet the President's request, you have got to have that worked out a whole lot sooner than that, because we have to produce a bill in subcommittee, full committee, House, Senate subcommittee, Senate floor, Senate conference, and get it to the President. If we can't get the numbers together, we are stuck with an inability to move this forward.

Mr. DUBE. That is one of the reasons why the Secretary is meeting with Mr. Murtha. I am confident we will not end up with a disagreement over the outlay values over the sources we have identified. That will be part of the discussion, and any agreement that the Appropriations Committee makes will be based upon having presented those to CBO and gotten their scoring on it.

Mr. OBEY. Mr. Edwards.

DEMOCRATIC INSTITUTIONS

Mr. EDWARDS. I certainly can't add anything to where the money is going to come from. I have a couple of questions, though, about where the money is going to go.

Secretary Aronson, in your comments you and others talked about what happened in Panama and Nicaragua and great achievements in securing additional democracy in the hemisphere. I think we all see it that way. I am supportive of the Administration's request, but I am concerned about the amount of money which is in both sides of the request, both Panama and Nicaragua, to help strengthen the democratic institutions in those countries.

As I understand it—and we could get into whether or not the money for education or other things helping to further that goal—but we have about $20 million earmarked in Panama's request and only $5 million in Nicaragua's request. It would seem to me that both of those countries, having come through long periods in which there was an absence of the essentials of democracy, whether we are talking about free press, free elections, or whatever they are, need a great deal of additional help in strengthening their institutions to make them permanent members of the democratic community.

Do you honestly believe that the $20 million for Panama and the $5 for Nicaragua are adequate to meet that purpose? If not, what do you see that needs to be done in the future on top of this? How do we help make democracy a permanent part of those two national entities?

Mr. ARONSON. Congressman, let me say a few things in response to your point.

First of all, the whole package, I think, has to be seen as strengthening and institutionalizing democracy. If these two new democratic governments cannot deliver to their people and meet what I described as a revolution of rising expectations, then confidence in the democratic system will erode and threats to the democratic system will get stronger. So I think that, I know you are making a more technical point about a specific set of programs, which I happen to believe in strongly, but I think that has to be kept in mind.

With regard to Nicaragua, as I said in the opening statement, we are talking about a long term development assistance effort which will be ongoing. The President has made it clear he intends to ask for a budget amendment for fiscal year 1991 of $200 million. We would expect that there will be a continuing democratic initiative component in that, the size of which I will not predict right now.

This $5 million with regard to Nicaragua should not be seen as the only amount. In Panama, as you know, we have already, in the initial $42 million, which the Congress, to its credit, approved in a very rapid fashion. We have already begun to provide training through both DOD and through ICITAP, I believe, for the new police force, which is a democratic institution building.

In Panama, is the most important institution to democratize to ensure the survival of democracy is the military, to wean them away from a previous existence as the overseer and dominator of the state, to that of servant of the state.

I think there are more resources on the Panama side because some have already been obligated. And with regard to Nicaragua, that will be an ongoing program.

Mr. SCHIECK. I think the initial estimate in the $500 million Panama package for an administration of justice program is as high as $20 million. We are still working with the Panamanian government to define the specifics of the program. We are going to be working with not only the police, but also with the security and lower courts in the country.

REPATRIATION OF THE CONTRAS

Mr. EDWARDS. One of the things which we are trying to do with the money that we are putting into Nicaragua is to bring about as quickly as possible the reintegration of the resistance into the Nicaraguan society, the idea being that with the war at a standstill, the Sandinistas having lost the election, there is no reason for the contras to avoid going back into Nicaragua and joining in the economy.

There is a dispute apparently as to who should be handling the funding of that repatriation effort. The Administration wants, I think, to be in charge of doing that. Would you tell us why does it matter who handles the money? Why is it important to do it as you propose?

Mr. ARONSON. Honestly, I don't think there is a dispute, Congressman. We have offered the International Controller on Verification Commission startup funds. It took them a while to develop a plan. They have not yet developed an overall plan. We are perfectly prepared to work with them and as they develop a plan, to allow them to administer and to share some resources. There is not really a quarrel. But we want to move this as expeditiously as possible.

We don't want bureaucratic or coordination problems between the UN and OAS or failure to develop a plan quickly to avoid holding up the process, for obvious reasons. Therefore, we want to obtain flexibility, if there is no plan, to do it ourselves. But there is not a permanent wall between us. If they get ready and they are prepared and they can handle this, we are not adverse to letting them play a role in any way, including using resources.

I think we showed that by offering funds out of the previously located money that was part of the bipartisan accord.

ADEQUACY OF AID PACKAGE

Mr. EDWARDS. I have just one other question. In the time since these numbers were put together, in an assessment of what was needed in Nicaragua, the Sandinista Government has continued to be in power and to do a variety of things that have an impact on that nation's economy. Are you comfortable that the numbers that you are submitting are sufficient for the time being or have new problems come up as a result of Sandinistas selling off oil supplies, some of the things they are doing about property being given to FSLM leaders, and so forth? Has that changed the numbers required in any way?

Mr. ARONSON. I think the more we look into the dimensions of economic problems in both Nicaragua and Panama, the more sobered we are by the dimensions of the challenge. We wouldn't be proposing these sums if we did not think they were adequate, but we have no illusions that they are sufficient to the task and they alone will do it.

I must say there is no fat in these numbers. I would just note, for instance, with regard to Nicaragua, that the socialist bloc, essentially the Soviet Union and its Eastern European allies, have provided upwards of $500 to $600 million in economic assistance every year to Nicaragua. We are talking about half that amount from the United States.

In Panama, as I said earlier, it is a little bit as if you owned a business that was-run by the mob for the last 20 years and you come back from a long vacation to start looking around for what is left and you find nothing but rubber checks. So these are not gold plated programs. These governments are going to need help from other donors.

On the other hand, it is important that the United States take the lead. We are not going to have credibility in going to the Japanese or to the others by saying Panama needs international support and Nicaragua needs international support, if we have not made a commitment.

Mr. EDWARDS. Mr. Chairman, I don't have any other questions, but I would make this comment. Some have criticized the Administration for moving timidly in responding to some of the changes in the world as they have developed. I think there is no question that in this particular case, in dealing with the changes in Panama and Nicaragua, which are the closest to us, the Administration has moved very boldly, has come up with a program that it would seem to me all of us could support.

Regardless of the battles that have taken place in the past, one of the important things that happened in the evolution in Nicaragua was when the Congress came together in a bipartisan way for these elections. I would hope that we would be able to meet the President's request to get this legislation passed as quickly as possible, while resisting all of the many attempts that are going to be made to turn it into a Christmas tree and attach everything that everybody wants to this bill.

There are always opportunities for other supplementals. I think the situation in Panama and Nicaragua requires that we resist those temptations in this case, and give the President as quickly as possible a clean supplemental on these two issues.

Mr. ARONSON. I appreciate those remarks. I would just like to stress also that obviously if the supplemental were passed by the Congress, the Administration would work with this committee and others as the funds are obligated and the programs go forward, as we normally do, and would seek the committee's views, and welcome the committee's oversight.

Mr. OBEY. I would simply say the committee will respond as quickly as it can, but we cannot respond until we have this matter we were talking about earlier cleared up.

Mr. McHugh.

DISARMING AND DEMOBILIZING THE CONTRAS

Mr. McHugh. Thank you, Mr. Chairman.

Secretary Aronson, I think Mr. Edwards speaks for all of us in saying that we will respond with some assistance to both Panama and Nicaragua. We have responsibilities all of us recognize. But it is important, as the chairman has said, for us to understand the details. He has raised an important question about the offsets.

I am not clear, frankly, about a number of things. One of them relates to the disarmament and demobilization of the contras. You have $32 million in here for that purpose. But it is not clear to me how that will be spent. It seems to me that the most serious potential obstacle to a transition of power in Nicaragua is this issue.

We would agree, I am sure, that the Sandinista Government should turn over power to Mrs. Chamorro, consistent with the election returns, but nonetheless, as a practical matter, we are hearing things which could pose a real problem. We are hearing that contras are infiltrating into Nicaragua with arms. I would be interested in knowing what your latest information on that is in terms of numbers.

We are hearing that the contras are demanding that enclaves be established within Nicaragua where they could relocate with their arms. Is that report true? We are hearing that they are calling for demobilization simultaneously—that both the contras and the Nicaraguan Army should demobilize. Is that true?

Most importantly, what are our specific plans to disarm and demobilize the contras and repatriate them? I certainly am more than willing to see us spend money for that purpose. I think it is important to do so. But I don't want to spend money without knowing how it is going to be spent.

What can you tell us about the specifics of this plan and, in the process, about the contras themselves?

Mr. Aronson. What we are trying to do is end a ten year old civil war. I think we are very close to doing that. This is obviously a difficult and sensitive issue. You should have no doubt about our will to make it happen.

We think it is time for the combatants to put their arms down and go back to normal civic life and take up their old lives. Many of them are peasant farmers. The question is, how do you make it happen? There is no button to push, there is no speech to give that will simply end ten years of fears and suspicions on both sides.

What we don't want to have happen is a standoff, with the Sandinista Government saying we will not turn over power until every contra has laid down his weapons and then the contras saying we will not feel safe in laying down weapons until the Sandinistas have turned over power. This would be a non-starter and a dangerous situation.

We have been trying to support the process established by the Central American Presidents, which envisions a large role for the UN in carrying out this process. The Security Council has just passed, or is about to pass, a resolution that we support to enlarge the mission and size of what is called ONUCA, the U.N. Central American Peacekeeping Force. That might include the addition of as many as 800 members that probably will come from Venezuela out of a battalion that had been prepared to go to Namibia to play a similar peacekeeping force.

We have our own views on this. I think it has to be negotiated between the parties. We have, from day one, taken steps to try to encourage the process. The President personally talked about this. The Vice President and Secretary of State met with the resistance leaders Friday to make our views known.

Mrs. Chamorro has sent a personal representative. The resistance has met with the CIAV. We have encouraged Cardinal Obando to play an active role because he is someone whom the resistance trusts.

There happen to be real fears that have to be addressed. As the Tela Accords provide the rights and freedoms and security of the resistance have to be provided for and some sort of a verification mechanism set up. That is something we believe the church and the CIAV can help play a role in. In fact, we provided funding to set that network up. It was envisioned under the accords in '88, a rural network established by the church.

The resistance returns home. They hook up after them. If there is a violation or abuse, they can report it.

We have to suggest to the various parties that a process begin immediately, first to separate the two armies so that there is no possibility of renewed violence.

There have already been some attacks in the North. Our information is that they have been started by the Sandinista Army.

They, of course, claim the opposite.

The important thing is to separate the armies so there is no chance of renewing the war and we hope that ONUCA can do that.

The question is, how do you separate the armies when a significant number of the resistance forces are inside the country?

So this idea of enclaves has emerged. It is not a new idea. It was negotiated between the Sandinista Government and the contras in 1988, in an agreement that both sides signed.

Perhaps the EPS would withdraw to certain designated locations. With ONUCA and them, the demobilization process could then go forward.

CONTRA ENCLAVES

Mr. McHugh. Correct me if I am wrong, but my understanding is that the idea the contras have is areas where they would control and retain their arms until April 25.

The idea of enclaves has been agreed to in the past, at least by the Sandinista Government and I believe by Mrs. Chamorro, enclaves controlled by the U.N. forces into which the contras would come and surrender their arms prior to April 25.

That is my understanding of the differences between what these enclaves mean in the eyes of the contras on the one hand——

Mr. Aronson. I don't think that the parties have gotten as far as you suggest.

I think the contras have a view, but whether that will be their final view when an agreement is reached, I can't tell you.

I think there is jockeying on both sides.

We want to get the process moving so the momentum and the direction is clearly going forward toward demobilization. The reason we want to start by separating the armies is we think that is the most important first step.

If the war resumes for any reason, we want them to know who started it.

We will say the Sandinistas.

It would be a disaster, so we want to get ONUCA in there, and enclaves is one way to do it.

Whether the resistance would from day 1 go into enclaves unarmed, I can't tell you.

I suspect right now, no.

They say we want our security guaranteed before we give up our weapons, but if you get a process going that is moving in that direction and the transfer of power is going at the same time, I think we can make this work.

Our package supports this in a variety of ways. We reprogrammed some old money that isn't in the supplemental to set up this verification network to give the contras some confidence.

We offered in the supplemental several million dollars as our share of the U.N. Peacekeeping Force to allow it to deploy immediately.

The economic package is an incentive for resistance forces to go home.

CONTRA AID AND SURRENDERING ARMS

Mr. McHugh. Is the economic incentive tied to the contras surrendering their arms? That is to say, will we examine economic aid to the contras on their surrendering arms?

Mr. Aronson. Yes.

Mr. McHugh. Is that anywhere in this package?

Mr. Aronson. I don't know.

Mr. McHugh. If we were to add language to that effect in some form, would that be a problem?

Mr. Aronson. To be honest with you, I would rather work it out in another form.

I just testified what our policy is and maybe we can have other ways of communicating it.

I understand your intentions are good, but someone elde is going to have another idea and somebody else in the Senate will have another idea and that is how a supplemental gets cut up in a lot of pieces.

Mr. McHugh. I don't doubt your sincerity, Mr. Secretary, but there is a certain degree of skepticism around the country and in the Congress as well——

Mr. Aronson. About our intentions—because that isn't warranted.

We spent a year on Nicaragua on this bipartisan accord and if our intentions are still suspect, then something is wrong.

Mr. McHugh. Well, Mr. Secretary, whether you like it or not, some people are skeptical, given the fact that the contras, during the period that the bipartisan accord was implemented, continued to conduct military operations in Nicaragua and there are those who connect our non-lethal assistance with those operations.

Mr. ARONSON. The food aid runs out in April so what we are talking about is not a renewal of the same maintenance aid. Maybe this will clarify it.

We are not talking about a renewal of the same program of humanitarian assistance where they stay in Yamales or inside and get food to maintain themselves.

This is a demobilization package that will allow them to be transported back to their home areas, but in exchange for them having given up a weapon which they wanted to do and intended to do.

We don't want to turn them loose in a devastated area with no way to support seven or eight kids.

Mr. MCHUGH. We are not questioning that, but there is a great deal of skepticism as to whether the contras who now have guns wish to surrender those guns and give up the possibility of further resistance if things don't go as they would like them to go in Nicaragua.

Our purpose and your purpose is to be sure that the contras give up their guns in exchange for which they get economic help.

We need to reassure people that that, in fact, is what will happen because there is some skepticism about the past, and I would like to be able to see us reassure people as expressly as we can.

This package of reintegration and demobilization assistance is meant to provide a new livelihood for unarmed resistance members who have returned under a process established peacefully to Nicaragua.

That is when they receive it. It is not to maintain aid for armed resistance members to maintain themselves for future periods of time.

Mr. OBEY. Mr. Lewis.

NEED FOR FLEXIBILITY IN SUPPLEMENTAL AID

Mr. LEWIS. Thank you, Mr. Chairman.

Welcome, gentlemen.

Mr. Chairman, let me say that I personally appreciate very much your expediting the holding of this hearing and I also want to compliment members of the Administration who have participated in attempting to fashion a package of assistance that will respond to the near-term crises that all of us recognize.

There is no question with the almost incredible changes taking place around the world, welcomed by all Americans is the movement toward peace and opportunity for democracy in Latin America and Central America.

I don't question that if this item came to the floor tomorrow after some extended discussion, it would pass overwhelmingly with broadly based bipartisan support.

Having said that, it seems to me, Mr. Aronson, that while we may argue within this committee as to how much flexibility the Administration ought to have in dealing with funding of the world, and the debate runs back and forth on whether we should have specific allocations of funds for some countries and not others, there is little doubt that as much flexibility as possible ought to be given to funds which are provided for this transition period to these two countries.

If we build in too much rigidity, we could defeat the purpose for which these funds are flowing.

I don't think there is any doubt about the purpose of the work that you have been so successful with in the last several months and the work with this committee as well.

It has been most positive.

If we could extend that attitude with this funding, I think it would help round out what has been a very successful venture for which you are due a good deal of congratulations.

Mr. ARONSON. Thank you.

It would be helpful to retain some flexibility in both packages.

We would obviously consult with the Congress, but you have brand-new situations in post countries.

Neither Panama or Nicaragua has ever faced the historic opportunity and challenges it faces today and we would not be serving those countries well or our interests if we simply hand-cuffed ourselves to a formula that we believe is right now, but six months from now we might want to take a slight turn.

We are not talking about some purpose of legislation, but some flexibility to move money among the accounts obviously with consultation beforehand would be a wise way to go.

REPATRIATION OF CONTRAS

Mr. LEWIS. There is without question some remainder of skepticism among people who are interested in these processes within the United States. There also is some skepticism remaining, I think, in the field of Central America.

A staff briefing indicates that in one instance where people were urged to come back to their communities in Nicaragua, of some 42 who came back voluntarily, 12 are dead. I understand that 23 are in jail and have been fined. I am not sure what happened to the other seven, but others in the field probably are skeptical as well.

These funds are designed to accelerate a transition process, and I hope that the Congress will recognize that we can't check every rifle in the field, but the purpose is the same.

Mr. ARONSON. You are referring to a survey that Commandante Johnson made. He did return during the election with our support, and then he went to try to check on, I think, 47 other members of the resistance who had come back. He found many had disappeared and others were in prison. That is a legacy that has to be dealt with here.

America's Watch did a report three months ago where they said, I think, 87 members of the resistance had been executed summarily in the previous year, and these peasants are not dumb.

They know how they have been treated for 10 years and they are suspicious and they have fears and they have to be addressed. There is no magic solution to this.

We also think that all parties want to achieve the same result and an economic incentive package to allow them to return to their normal life while their security concerns are being addressed, will be a way to resolve this peacefully.

Mr. LEWIS. It seems that we have had a real demonstration of success in recent months, with this committee and other committees with good faith working closely with the Administration.

State and AID have been extremely responsive. I hope that we can try to extend that as these months flow forward.

NICARAGUAN AGRICULTURE

In the near term we really do have a crisis in the field in Nicaragua. The growing season is shortly before us. We should have already played a significant role in terms of identifying the numbers of acres that ought to be a part of an aid process. The identification of the volume of seed, grain, and pesticides ought to be going forward right now.

What has been done since this item came up in hearings last week? Are we moving in the field?

Mr. SCHIECK. Congressman, we have been informed by the current government in Nicaragua that they will give visas to us to travel, and we plan to leave this week.

There is a team scheduled to leave on Thursday which will include agriculturalists to look into the questions you have raised.

We are also concerned about the timing of our assistance. It is relatively easy to buy fertilizer. However, the issue is, what happens when the fertilizer reaches Nicaragua? How will it be distributed and how will it reach the farmer? Under what terms will the farmers be asked to pay? These are the kinds of issues the team must address.

We don't know much about it because we haven't been there for many years.

When the team returns the following week, we expect to have many of the answers to the questions you have raised. Those answers should help us know how to proceed to get fertilizer into the country before the growing season starts. The target is to have the fertilizer arrive before the end of April.

Mr. LEWIS. We have heard reports that organized groups within Nicaragua are suggesting that there is not evidence of a quick turnaround.

Are you confident that we are going to be able to actually be the jump-starter in this connection and get that material to the field quickly enough?

Mr. ARONSON. Well, the President has already taken some steps initially, lifted the embargo and all of the trade sanctions. We are talking to the new government about their becoming eligible for GSP and CBI. We are trying to work on assuring their sugar quota.

This is a huge task. The President is very serious about this, and we are going to mobilize the resources of the administration.

I think this is a place where the American private sector could make a great contribution as well—the farmer cooperatives and agribusinesses who could make a big contribution at small cost to themselves in Nicaragua if they wanted to.

Maybe Members who have access to these people might encourage them to do so.

Mr. **Lewis**. We are talking about a matter of weeks and it will be so much blowing in the wind unless we have specific action items.

I would hope that this is being treated with the highest level of urgency in terms of production, moving right now.

Mr. **Aronson**. We are sending down our economic team to Nicaragua this week to look over the ground. This area is the one that we and they are concentrating on.

This is an agricultural-based economy. The planting season begins in April and the rainy season begins in May, and if they are going to increase acreage and crop yield and planting, they need to know now what is going to be available.

So we want to do what you are urging us to do.

PANAMANIAN FOREIGN ASSISTANCE

Mr. **Lewis**. Mr. Chairman, the last comment I would make is that people who have recently talked with me about Panama, talk about the shift in atmosphere in which there is very positive response on the part of Panamanians regarding the role the United States has played in the last several months.

Popularity of Americans in Panama has not always been high. If there is a hole in our foreign assistance in that general region, it is that "Yankee go home" is not simply ever-present, but there is reason for its presence.

I hope that in your thinking in the State Department, as we undertake emergency assistance, we will rethink the way we can impact the way in which capital flows to those countries. Our foreign policy should be long term and build a foundation which will provide opportunity for the poorest of the poor in those countries, so that democracy means more than just going to bed hungry.

Mr. **Aronson**. That is good advice. I will give you an opportunity to help us.

We are trying to expand the provisions of the CBI through which Panama and Nicaragua will benefit with some modest changes that will allow certain apparel and sneakers to be produced there from patterns produced and cut in the United States.

We didn't get it through the Senate Finance Committee for the usual reasons, but we would love to see it strengthened in the House, because it is poor people working in those little factories.

Mr. **Lewis**. Let us not be timid.

Mr. **Obey**. Mr. Lehman.

OVERSIGHT OF PANAMA AID

Mr. **Lehman**. Thank you, Mr. Chairman.

We are going to, in this legislation, provide several hundred million dollars to Panama. How can we be sure that this money does not end up with the kinds of people that were involved in the drug economy, which was a large part of the financial resources in Panama for so many years?

Are you going to follow the money to Panama to be sure that it doesn't end up as a farmer's assistance program for the drug trafficking?

Mr. **Aronson**. Definitely. We are going to have the normal auditing, oversight on all of these funds.

I might add, on the issue of drug trafficking, that this government in Panama is led by three men, all of whom were victims of narco-trafficking in Panama. The corruption and the funds that were used to sustain this dictatorship in part came from drug trafficking and they were victims.

I would note three actions that the new government has already taken to assist in combating money laundering, which is one of the areas that is important to focus on. In December, at their own initiative, they offered to freeze any bank accounts that we thought were potentially involved in criminal investigations, and at our request, they froze several hundred.

In February, the cabinet of the Endara government passed decree 41 which mandates that any cash transaction of $10,000 or more or transaction in certain negotiable securities have to be recorded and the identify of the customer defined. That is something we have in our own banking law. They didn't have it before.

They have now put it into effect pending legislative approval, and the Supreme Court recently ruled that the Attorney General has the authority to go into coded bank accounts and get the identity of customers for law enforcement purposes.

Finally, this past week my principal assistant, Mike Kozak, and a team from Treasury and Justice has been meeting with the Panamanian government negotiating an agreement with regard to money laundering in particular where we would be able to share this information.

So I think we are as concerned as you are about it and trying to take steps to make sure we support the Endara government's effort to prevent this.

SOVIET REFUGEES IN ISRAEL

Mr. LEHMAN. The 1991 budget requests $30 million to resettle Soviet Jews and others in Israel. You recognize that with the numbers increasing, the needs have also increased. Before we were dealing with 1,500 Soviets per month; now it is 6,000 per month and going up.

We recognize that you can't plan ahead for all of this. In fact, we had Peres before us in October and he was optimistic about exceeding 100,000 Soviets to Israel over the next three years. Five months later, that number may be reached in the year 1990 all by itself. We have sort of been caught short.

Wouldn't you agree that we have an emergency with regard to this refugee problem on our hands at the present time?

Mr. LYMAN. No question that the increase in the numbers going to Israel places a great financial responsibility on both the Government and private contributors.

Our grants have always been a very small part of the total. Our grant of $25 million compares to a UIA program of over $300 million.

We have had to plan our budget in terms of a lot of other requirements we have, and at this point we don't have plans to increase that particular portion of the budget.

Mr. LEHMAN. Mr. Chairman, I have one other question for the record and I want to thank you for the time.

[The information follows:]

HEALTH ACTIVITIES IN NICARAGUA

Question. To what extent does A.I.D. plan to work through non-government organizations in carrying out the health activities in Nicaragua ($35 million)?

A.I.D. Response. Following years of civil war and a decapitalized economy, basic medicines, supplies, and equipment are urgently needed in Nicaragua. The purpose of A.I.D.'s medical and health assistance is to begin to provide essential health related requirements to a highly centralized, well-organized health system. This activity is designed to be implemented rapidly and to take in two phases.

During the first phase, which is within the existing legislative and budgetary authorities, $4 million is being made available on a competitive basis to private voluntary organizations (PVOs) for the purpose of providing curative care to victims of the civil war. This activity is expected to begin before the end of April, 1990.

A much larger program is being designed to provide technical assistance, training, and essential medical equipment, pharmaceuticals, and supplies to improve the existing health care delivery system in Nicaragua. The breadth and depth of this program has not yet been determined; however, it is anticipated that PVOs will continue to play a significant role in the program.

Mr. **OBEY**. Mr. Mrazek?

DISARMING AND DEMOBILIZING THE CONTRAS

Mr. **MRAZEK**. Thank you, Mr. Chairman.

I want to apologize for getting here a little late today. I hope I am not covering ground that has already been covered.

I did hear the last of Mr. McHugh's questions.

I would like to have you confirm the statement that none of the $32 million proposed would go to armed contras or contras who are still in a state of military preparedness.

Did I understand you to say that?

Mr. **ARONSON**. Correct, although there might be a process where they are laying down their arms and they already get a ticket or something.

The answer to your question is there won't be any.

The purpose is to allow them to return to civilian life unarmed.

Mr. **MRAZEK**. Could you perhaps discuss the length of time that is anticipated for the process of demobilization and repatriation of the contras?

Mr. **ARONSON**. That is difficult to say.

We would like it to move along as quickly as possible, and I think Mrs. Chamorro would like it to move along as quickly as possible.

The question is how do you create a process where there is confidence and it can move forward.

We have tried to work with the Central American Presidents and with the U.N. to create that process.

My own sense is that the vast majority of these peasants in this army want to go home. They don't want to go back to war, but they are somewhat skeptical and justly afraid.

From their point of view, just so you understand their thinking, they have seen this movie before.

They remember in 1979 when they also saw Violeta Chamorro, who was then part of the junta, and the Sandinistas negotiating and there were a lot of promises and then for the next 10 years they were subjected to a very oppressive and terrible dictatorship.

I think that the process needs to begin, I think it already has begun in its own way through the discussions that I described.

We need to create facts on the ground that keep leading in the same direction.

That is why we talked about separating the Armies.

Congressman McHugh seemed to be suspicious of the idea of enclaves, but this isn't some device to stall demobilization.

It was, in fact, the designated means that the Sandinistas and contras agreed on the last time they discussed demobilization and they contemplated as the first step that they go into the enclaves with arms, but then demobilize and go back to their home areas.

Whether that is the way it works, I don't know. We need to negotiate something.

We hope it will start right away.

I think there has been more demobilization than people realize.

I think a lot of the leaders have gone home. I am not sure they are an organized menace anymore.

CONTRA BASE CAMPS

Mr. **Mrazek**. That brings up another point involving the fact that for the last year or so there have been reports by various human rights organizations, health workers and volunteers that a number of young Nicaraguans were taken against their will, both young men and women, by the contras and are being held against their will in some of the base camps along the border in Honduras.

We have received reports as late as last month that somewhat surrealistic conditions as far as information flows still exist in some of those base camps, and I am just wondering whether there is a way that you could envision a structure being created in which either the UNHCR or some other international organizations would have an opportunity to have access to those camps; not to compromise their security, of course, but to interview people who might be willing or desirous of leaving right now and don't feel free to do so.

Mr. **Aronson**. I know something about that personally because I once talked to the Sandinistas about it, and what they told me privately is that they honestly don't believe there are any people being held, but there is a list of 800 Nicaraguans whom they presume were killed in combat, but they haven't confirmed this because they didn't want to pay the political price of telling their families about that or that they went over to the contras.

So they have kept alive the idea that they were kidnapped.

In fact, in negotiations in November, the resistance agreed to allow the Inter-American Commission on Human Rights to come and explore the camps and to interview anybody who was considered to be one of these people and they made it clear they would allow that to happen.

I think under the demobilization process, the CIAV will conduct a census and there will be access to the camps.

We would certainly encourage that and I think the resistance agreed to that back in November.

I don't think you will find anybody there, based on what the Sandinistas told me, but to the extent to which there are concerns they ought to be addressed——

Mr. **Mrazek**. I wasn't really talking about people that the Sandinistas have spoken about, but rather the accredited international human rights organizations.

A list that I was privy to was nowhere near 800. It was more in the neighborhood of 100 to 150. A couple of doctors interviewed five of the people and three wanted to leave and then a contra commander reversed his decision and they weren't allowed to leave.

These were young women, and I don't know what value they had to the Nicaraguan freedom fighters—actually, I could see value that they will perceive. But we are not talking about information from the Sandinistas now. We are talking about information international health organizations and human rights organizations.

Mr. **Aronson**. Do you remember what the name of the group was that made these claims?

Mr. **Mrazek**. I could apprise your office of that. I am hoping in the interest of clarifying the situation that those camps could be opened up to some international monitoring.

Mr. **Aronson**. I think they will be as part of the process of demobilization because I think one of the early steps proposed is a census of the camps, and if you want to forward us the list, we would be happy to make sure that that is integrated into the process.

My experience has been that some of those lists tend to be politicized in a certain way and there are different stories, but if there is anybody being held in any fashion, they shouldn't be.

Mr. **Mrazek**. Thank you.

HEALTH PROGRAMS

Mr. Schieck, are there any proposals to spend any of the money either in Nicaragua or Panama on what we would call child survival programs, programs designed to assist children who might have lost parents or otherwise had their lives significantly damaged?

Mr. **Schieck**. Yes, sir.

In Nicaragua, there is the $4 million which was previously appropriated by the Congress for the CASA program.

We have asked for expressions of interest from U.S. private voluntary organizations for proposals on how they would administer such a program in Nicaragua.

Previously, we could not do that. The Sandinistas would not allow PVOs, to operate in country with U.S. Government Funds. We have now asked for proposals and I am confident we will get a number of good ones for this purpose.

Secondly, we are proposing, with the passage of the supplemental request, to reopen the type of health programs AID is doing in many countries around the world. These programs basically try to improve health outreach to rural areas.

In Nicaraguan, this program would include purchase of medicines and equipment to make sure that the health system is adequately supplied to administer on effective program.

In Panama, we are not planning to focus on health programs, other than perhaps of repairing infrastructive such as hospitals which may have deteriorated over the last few years due to lack of maintenance.

The health status of the people of Panama is quite good compared with other people of the region. Therefore, we do not propose to fund any extensive health program.

Mr. ARONSON. There is food aid in the initial package that was previously obligated funds and in this package which will help with the nutrition issue.

Mr. OBEY. Mr. Coleman?

BUDGET DEFERRALS AND OFFSETS

Mr. COLEMAN. Thank you, Mr. Chairman.

I wanted to get back to the source of some of the funds, Mr. Chairman.

I understand that this is not something that the witnesses before us can testify to other than to let us know maybe with a bit more certainty, about where the money is coming from.

The gentleman from the Office of Management and Budget referred to maybe the difference as being in the outlay numbers. In other words, the differential depends on whether or not they had taken into account the deferrals in one instance and not in the other.

OMB had taken into account deferrals sent by the President.

Are you referring to the deferrals sent by the President—the $425 million in budget authority mentioned to us in his speech of February 6? Is that the group you are talking about?

Mr. DUBE. A total of $2.2 billion in deferrals.

Mr. COLEMAN. They called them excess Panama outlays, $425 million, and I am wondering if that is under a subheading called Excess Panama Outlays.

Mr. DUBE. That was merely the amount by which, based on OMB's estimates, the outlays from the deferrals and the budget authority sources that we submitted for the Panama supplemental exceeded the amount of outlays required for Panama.

Mr. COLEMAN. The problem is that even in the document that I have, and I suspect the document may have been prepared in the Department of Defense because we got it in the Military Construction Subcommittee it refers to sources for Nicaragua. In fact, I guess that is the only title this one had.

They showed that an outlay number of $72 million was the difference, and the problem with the numbers that we have already seen is that there's a difference perhaps, of more than that.

I am just wondering if we are talking about the same thing or whether or not those numbers are still skewed somehow.

Mr. DUBE. I haven't seen a CBO document in which they have scored them. These presumably were provided to us by OMB as being the amount in the package submitted on February 6, the outlays identified by OMB being saved as a result of a certain budget authority.

Transfers that we proposed and the value of the outlay savings associated with the deferrals that the President had proposed exceeded the requirement for outlays for the Panama supplemental by $78 million and, therefore, as we were trying to offset the Nicaragua supplemental, we needed to come up with $300 million in budget authority and a smaller amount of outlays because of that other amount.

That doesn't catch up to the subsequent CBO scoring of it, and I don't have that.

Mr. COLEMAN. I was told that this document that we had received last week was no longer operative or valid because of the fact they were taking these under advisement, reviewing them all over again, that some of these met with disagreement within the administration, I understand.

It certainly met with some in the Congress, I know.

Mr. DUBE. That is correct, and based on that we have a set of account numbers that were proposed in the supplemental which are part of the negotiations that will occur in order to try to reach agreement on the projects and the accounts from which we are taking money, whether it be military construction or other accounts.

Mr. COLEMAN. To project the total amount—was that——

Mr. ARONSON. Eight hundred million.

Mr. COLEMAN. That total amount, nonetheless, we use the term offsets. I am worried that we may be using those a little loosely, because if we are going to include deferrals, whether or not we are going to do any reprogramming, it seems to me we should be fairly specific about those, because it becomes important to other committees and to other Members in the Congress as to what we are doing.

Do you agree with that, Mr. Secretary?

Mr. ARONSON. Yes.

When the President decided to add the Nicaragua package to the Panama as one supplemental, he directed the Secretary of Defense and the Director of OMB to review and come up with a proposed set of offsets for the entire package, and they and their designees will be up here briefing the committee, including this committee—I believe at the staff level that may have already begun—but I will take the message back that the chairman and the committee would like to get a full briefing on that.

That process has gone forward and I think the only problem is that the political and economical people came today and we weren't aware that you wanted somebody to speak to that issue.

If we had known, we would have brought somebody from OMB. It is just that the wrong set of characters came for your questions.

Mr. DUBE. Mr. Diefenderfer and Mr. O'Keefe met with the staff of the full committee on Thursday, both the House and Senate, and that is proceeding.

Again, as I said, Mr. Chairman——

Mr. OBEY. If I could clarify with respect to the deferral package, isn't it true that the GAO has determined that the deferral package submitted by the President is in violation of the Budget Control Act. It is, therefore, off the table in terms of a possible source for the offsets that you are talking about?

Mr. DUBE. The programs themselves are not off the table because if the issue here is related to the deferral, if we can reach agreement with respect to congressional willingness to rescind those funds or to deappropriate them for the purposes of offsetting the Panama or Nicaragua supplemental, that would moot the question of deferral and represent a budget authority source that could be used——

Mr. OBEY. But there are many things we can do if the Budget Act and Gramm-Rudman were changed, but GAO has determined they deferrals are in violation of the Act. Isn't that right?

Mr. DUBE. Yes, sir.

Mr. OBEY. Thank you.

Mr. COLEMAN. It does seem to me that while we say that we are ready, as one Member of this committee who is being asked to vote on a bill hopefully in early April, as Mr. Lewis pointed out, a lot of us believe there are certain elements of this program that are important, some more important than others. I certainly would say that I am not so sure that the Administration has these numbers worked out.

The problem with including deferrals in sending us a package, in any event, scoring them now, is that it is fraudulent. You can't score them now because Congress hasn't agreed we are going to accept the deferrals.

I say until we do, let's not take that position. That is exactly how we get accused of using the worn-out phrase "smoke and mirrors."

I think we need to actually see the money and where it is coming from before we move on these things.

I am not going to vote to increase the deficit for these programs unless that is what we are going to tell the American people.

You all need to come here, as far as I am concerned, and if you want to borrow the money to pay for these programs, then let's say that.

If we are going to raise taxes to pay for these programs, let's do that. But for us to say these come out of deferrals that Congress hasn't yet enacted—so that when we don't enact them, we are put into the position of being at fault for not funding dollars for these countries, is not fair to the American people.

Mr. DUBE. Could I clarify one point——

Mr. OBEY. Do it quickly, because I have to be out of here at four and I have a series of boilerplate questions I have to get to.

Mr. DUBE. Our proposal related to the deferrals is not to score them as deferrals, but to cancel the budget authority for the programs that we mentioned.

So they would not be deferrals in that sense, but would be rescission or cancellation of budget authority like any other program.

Mr. OBEY. If the Administration is looking for cooperative and rapid disposition of this package on the part of the Congress, the Administration needs to start with a cooperative mindset with respect to offsets which it targets for oblivion. I do not think that we especially add to the ability of the branches of government to cooperate when the Administration starts by targeting items which were specifically added by the Congress in the budget cycle in the first place.

No Congress since 1946—I will repeat this figure a thousand times until people start recognizing it—has changed any President's budget by 2 percent or more. If the President is going to talk about deferrals, he ought to take a look at the 98 percent of the budget which came down his way, not the 2 percent of the budget that did not.

That is the only point I will make.

AFRICA $30 MILLION FUNDING

Let me get to other questions about the numbers. In February, Congress approved legislation which permitted the transfer of $30 million in ESF funds from Somalia and Sudan to Panama. This was done after reaching an understanding that the $30 million in funding that was transferred from Africa would be replaced as part of the $500 million Panama supplemental.

Can you tell us, is it the Administration's position, therefore, that the supplemental should include $470 million for Panama and $30 million for Africa?

Mr. **Aronson**. Fortunately, I had a conversation with Secretary Eagleburger this morning who negotiated that deal and this is what he told me our position is, that should the Appropriating Committees decide to make the African accounts whole by taking $30 million out, we would not oppose that action.

We are not coming here telling you or urging you to take the action.

Mr. **Obey**. That would not be regarded in any way as reneging on the Congress' part?

Mr. **Aronson**. We will live with your wisdom, Mr. Chairman. I have been instructed to tell you that.

Mr. **Obey**. It is not my wisdom. That is the agreement that was made originally, in return for the first supplemental. If Congress did that, it would be consistent with the agreement made on the first supplemental. Isn't that right?

Mr. **Aronson**. It would be.

Mr. **Obey**. All right.

ONUCA AND THE CONTRA AGREEMENT

With respect to Mr. McHugh's question, the ONUCA plan presupposes the contra agreement prior to deployment of peacekeeping forces. Will those ONUCA forces actually be deployed to Nicaragua without the contra agreement?

Mr. **Aronson**. Some of them, the unarmed forces, I believe, are already on the ground and operating. I don't believe that in the first stage, which is the separation of forces in the cease fire, any new agreement is necessary because the contras have already agreed to a cease fire and to ONUCA separating the two. I believe they could deploy on that basis.

You are correct that the U.N. takes the position that they will only carry out a demobilization process, particularly a disarmament process, with the agreement of the army that they are going to disarm. They are not going to do it in a hostile way.

I don't think that that will prevent ONUCA from deploying early to start the process.

Mr. **Obey**. If the contras do not agree, how in fact can that disarmament take place?

Mr. **Aronson**. I am sorry?

Mr. **Obey**. If the contras do not agree, how will that demobilization take place?

Mr. **Aronson**. In the Bipartisan Accord, I always talked about voluntary demobilization. Unless we are going to send somebody's army to try to subdue the contras and take away their weapons through combat, it is going to have to be some kind of process where we convince the resistance to take part.

CONTRA DEMOBILIZATION

Mr. **Obey**. My concern is this. I do not think anyone is suggesting the potential for bad faith on the part of the Administration. I certainly think that potential is there and then some for certain segments of the contras because, very frankly, while many of them may want to go back to Nicaragua, I think many of them are not going to want to go back to begin a life of farming. There are many people who, frankly, at this point, having spent a fair number of years doing what they are doing now, don't know how to do anything else. That is habit.

My question is, without assurances that they are in fact going to cooperate, how can we approve the money that you are asking for?

Mr. **Aronson**. Well, it is kind of a chicken and egg process. I would argue the opposite. Giving us the economic incentives will help us to convince them to cooperate and help convince the vast majority, hopefully, to mobilize. It will be a genuine economic incentive.

I think a vast majority of the combatants want to go home. But knowing they are going home to something as opposed to going home to nothing, I think, might make a difference. There is no way this package will be an incentive to keep from demobilizing.

As I told Congressman McHugh, the agricultural implements and the transportation and the seed and the fertilizer and whatever else for them and their families goes to them when they demobilize. It is a tough issue.

How do you convince an army to go back home? We are trying to create a process, support a process that will allow them to come to this decision in a way that they feel secure in doing, but also creates as many incentives for them to do so as possible.

Some of those may be necessary to talk about in private as well.

CIAV

Mr. **Obey**. What is the status of the $3.6 million now held in reserve by A.I.D. for the U.N.-OAS resettlement organization?

Mr. **Aronson**. For CIAV?

Mr. **Obey**. Yes.

Mr. **Aronson**. Basically we have offered, I think, a total of 3 million to the CIAV. I think 500,000 of that is going to the OAS already.

CIAV is developing a plan for start-up administrative costs for the rest. As soon as it is done, they will get the money. It took them awhile to get together, the U.N. and OAS, but they are pretty close.

PANAMANIAN BANKING AND MONEY LAUNDERING

Mr. OBEY. Bring us up to speed on another matter with respect to Panama. As you know, there have been a number of questions, and you referred to some of them today, about Panama banking practices and laws.

The New York Times has an article, somewhat dated now from February 6th, which mentioned the following facts. A senior State Department official here, who asked not to be identified, said existing laws are grossly inadequate to prevent money laundering—the process in which illegally earned profits are deposited in bank accounts or legitimate businesses, and withdrawn as clean money.

It went on to say American law enforcement officials and legislators are concerned that the new government and the country's appetite for foreign investment will lead to greater use of Panamanian financial institutions to conceal illegal drug profits.

Also, many of the senior leaders in government, while never accused of money laundering, have had strong ties to corrupt banks. Then the article mentions, without suggesting that the officials had any direct knowledge, President Endara, Vice President Ford, and Attorney General Cruz.

Can you give us a status report on what the situation is with respect to those banks, with respect to the associations those gentlemen have with those banks? Can you tell me whether things have changed enough since this article was written to justify putting that concern on the back burner?

Mr. ARONSON. I wouldn't put the concern on the back burner, Congressman. I think that every sign that we have seen shows good faith and concrete effort on the part of the new government to strengthen its capacity legislatively and administratively to deal with money laundering.

As I mentioned, even in December they voluntarily froze 200 to 300 bank accounts that we thought might be germane to criminal investigation. They didn't have to do that. They asked us if we wanted to do that.

Secondly, the cabinet issued a decree which requires that all cash transactions $10,000 and above be recorded and that the name of the client be confirmed. We have put that into effect here. That is one of the best tools with regard to attacking money laundering because it is large cash transactions they are looking for. That didn't exist before. It requires legislative approval. I think that is going to follow.

Third, as I said, the Supreme Court of Panama recently ruled that the Attorney General has the power to go into coded bank accounts and get any information necessary to law enforcement.

The fourth point is that we are currently negotiating a series of agreements, bilateral agreements with the government of Panama, that will permit us to share this kind of information when we need it for criminal investigation that we are conducting on our own.

Mr. OBEY. Have there been any divestiture actions taken by the three gentlemen?

Mr. ARONSON. Yes, there have been.

I would like to make one point about that article. I appreciate the fact that you noted that it said there was no personal involvement. There is a very clear statement in the article which said that nobody—part of the new journalism is if you want to get on the front page of The New York Times, impugn the integrity of somebody who serves in government.

Mr. OBEY. With all due respect, I do not think they did.

Mr. ARONSON. The headline did, Mr. Chairman. I thought it was a bad story myself because these three guys are pretty honest.

Let me read you a letter that speaks to the issue. It says, "Dear Mr. Chairman, I am writing with reference to your letter of February 13, 1990 to the Secretary." This is a letter to Larry Smith, Chairman of the Committee on International Narcotics Control.

"I am writing with reference to your letter of February 13, 1990 to the Secretary and my interim reply of March 6, 1990 concerning reports that linked high-ranking officials of the government of Panama with banks allegedly involved in money-laundering activities. Ambassador Hinton discussed this matter with President Endara, Vice President Ford and Attorney General Rogelio Cruz. Each of them denies any personal knowledge of money laundering by the banks with which they are or were associated, as well as personal involvement in illegal activities.

"I note The New York Times story of February 6, 1990, which I believe first surfaced this matter in the United States, said that there is no evidence that President Endara, Vice President Ford, Mr. Cruz or other current leaders are aware of or involved with other operations with the illegal operations carried out at the banks to which they have ties.

"President Endara is and was a member of the Board of the Banco Inter-Oceanico de Panama. It is not illegal for a President in Panama to so serve.

"Vice President Ford no longer serves on the Board of Dadeland Bank. He says he never was a part owner, but he once held stock options.

"Attorney General Cruz says he was a director of First Interamerican Bank from 1985 to 1987. Mr. Cruz states Noriega invented money-laundering charges against him in an effort to embarrass him because he was a long-time political foe of Noriega. After Mr. Cruz left the Board, the bank was intervened by the Noriega regime and is no longer functioning.

"We see no reason to infer wrongdoing on the part of President Endara, Vice President Ford or Attorney General Cruz"——

Mr. OBEY. I do not think that is the question. No one has inferred any wrongdoing on their part. What we are asking you is, what are the financial arrangements with respect to those gentlemen and what are the financial arrangements with respect to the banks in question that would lead one to be confident about the future?

Mr. ARONSON. I will have to get back to you in writing on that. I do think this is a little bit of a case of them proving they are not guilty. We will respond in writing to it.

[The information follows:]

I submit for the record a letter to Chairman Smith addressing this question in detail. As indicated in the letter, Vice President Ford and Attorney General Cruz no longer have positions with banking institutions. President Endara, acting according to accepted Panamanian custom, has maintained his position on the board of the Banco Interoceanico de Panama.

The greatest assurance we have that Panama will not resume money-laundering operations is the recognition by Panamanian government and banking authorities that such operations damage the country's interests. After all, money-laundering functions were a major source of the revenue that permitted the Noriega regime to sustain its dictatorial rule. Such operations also severely undermined the country's international image. Senior Panamanian officials have stated to us that they consider money laundering a threat to their national security and are approaching it as such.

The present Panamanian administration has clearly demonstrated its determination to suppress illegal narcotics and money laundering. I submit for the record a fact sheet setting forth the impressive concrete steps they have taken to date. I would note finally that the issue is not simply one of political will; effective enforcement requires resources. The $45 million included in the assistance package we are seeking will be used in part to provide training and equipment needed by the regulatory and law enforcement agencies of Panama charged with enforcing the strict new measures the government has adopted.

United States Department of State

Washington, D.C. 20520

MAR 21 1990

Dear Mr. Chairman:

I am writing with reference to your letter of February 13, 1990, to the Secretary and my interim reply of March 6, 1990, concerning reports that linked high-ranking officials of the government of Panama with banks allegedly involved in money laundering activities.

Ambassador Hinton has discussed this matter with President Endara, Vice President Ford, and Attorney General Rogelio Cruz. Each of them denies any personal knowledge of money-laundering by the banks with which they were or are associated, as well as any personal involvement in illegal activities. I note that the New York Times story of February 6, 1990, which I believe first surfaced this matter in the United States, said "there is no evidence that President Endara, Vice President Ford, Mr. Cruz or other current leaders were aware of or involved with the illegal operations carried out at the banks to which they have ties."

President Endara was and is still a member of the Board of the Banco Interoceanico de Panama. It is not illegal in Panama for a President so to serve. He sits also on a number of other Boards.

Vice President Ford no longer serves on the Board of Dadeland Bank. He says he was never a part-owner, but he once held stock options.

Attorney General Cruz says he was a Director of First Interamericana Bank for less than two years in the period 1985-87. Mr. Cruz states that Noriega invented money-laundering charges against him in an effort to embarrass him because he was a long-time political foe of Noriega. After Mr. Cruz left the Board, the Bank was intervened by the Noriega regime and is no longer functioning.

We see no reason to infer wrong-doing on the part of President Endara, Vice President Ford, or Attorney General Cruz. The Endara administration has repeatedly expressed its determination to prevent Panamanian banks from conducting money-laundering operations and has cooperated closely with us on narcotics issues. Not only has President Endara publicly

The Honorable
Lawrence J. Smith,
Chairman,
Task Force on International Narcotics Control,
House of Representatives.

denied the type of allegations contained in the New York Times article, his government has acted decisively. Shortly after taking office, for example, it froze some three hundred bank accounts suspected of being related to money-laundering operations. It has begun to exchange information with U.S. agencies and has asked for additional suggestions as to how we might make our cooperation more effective. In fact, at the invitation of the Panamanian authorities, U.S. representatives in Panama are negotiating several agreements that would strengthen and formalize our cooperation. Thus, we are convinced that the government of Panama is moving aggressively to keep the country's banking system from conducting money-laundering transactions.

I hope that our briefings and this letter will serve to put these allegations to rest. We would, however, be pleased to respond to any further questions you or your staff might have.

Sincerely,

Janet G. Mullins
Assistant Secretary
Legislative Affairs

Enclosure:
Article from the New York Times.

FACT SHEET: GOP PROGRESS IN COUNTER-NARCOTICS EFFORTS

Since the Endara Government took office, senior GOP officials and the President of the Banking Association of Panama have publicly expressed their view that money laundering through Panamanian banks is harmful to the Panamanian national interest and have stressed their intention to cooperate with the USG in efforts to combat money laundering.

GOP Officials Public Statements Against Money Laundering:

- In a February 7 television interview, Vice President Ford said that "The Panamanian Government will eliminate all mechanisms for laundering money in Panama. Much has been said about amending the law. We are determined to amend any article in the banking law in order to eliminate the problem of money laundering. ... banking secrecy ... is a juridical myth here. No bank secrecy law exists in Panama. In Panama there are only bank mechanisms whereby the courts have access to any type of bank account. So let it be understood once and for all. This Government will put right the banking system because it is good for the nation to improve its image. We will establish all controls necessary to prevent money laundering in Panama.

- In a La Estrella de Panama interview of February 25, Edgardo Lasso Valdes, the President of the approximately 100 banking institution Banking Association of Panama (ABP), stated that banks operating in Panama which are members of the ABP will cooperate with the national government to prevent the laundering of money derived from drug trafficking. Lasso further stated that Panamanian legislation offers no protection to customers implicated in crimes "and their accounts are subject to investigation by the appropriate judicial organizations ... " He said that even the most secret accounts within the Panamanian banking system, the "coded accounts" are subject to investigation.

- In a January 15 press statement, Deputy Government Minister Ramon Lima stated that to the extent that there are bank accounts linked to drug trafficking "Panama will cooperate with the United States to help the fight against them" and will begin checking the accounts. He added that the only people who should be concerned are the drug traffickers who "used the banks established in Panama to launder their money" and that other clients of the banks "can rest assured" because the GOP would respect their banking confidentiality.

The Endara Government has taken a number of concrete steps to match these words with deeds in combatting narcotics trafficking and money laundering activities in Panama.

Investigations under Panamanian Law, and Sharing Information with USG:

- o The GOP's aggressive new interpretations of its drug laws to obtain money laundering information and to then provide it to other countries' law enforcement officials are already showing concrete effects.
- o In December, the GOP froze over two hundred bank accounts believed to have been used for laundering drug money (based upon information provided by USG law enforcement agencies).
- o Victor Aldana Aparicio, of the Attorney General's Office, has said with respect to the frozen accounts that "the most important thing is the information we obtain, as it allows us to follow the trail of money from drug trafficking." The Panamanian Attorney General is now in the process of providing the information obtained about these accounts to US law enforcement officials for use in US investigations, and is working with US prosecutors to certify the records so they may be admissible in US courts.
- o In two recent decisions, the Panamanian Supreme Court ruled that the Panamanian Attorney General has the authority to compel the production of information about bank accounts including coded bank accounts from the banks for law enforcement purposes.

Law Enforcement Discussions:

- o In late February, the GOP requested the commencement of law enforcement discussions with the USG, in particular discussions regarding an exchange of information agreement.
- o At Panamanian invitation, we began discussions on a range of law enforcement agreements with the GOP, including an agreement establishing formal mechanisms for obtaining evidence, including bank records, needed in criminal investigations and prosecutions. These discussions are underway and both the GOP and the USG are keeping them on a fast track.

Currency Transaction Reporting Requirements:

- On February 13, the Panamanian Cabinet passed Decree 41 requiring the National Banking Commission to issue regulations requiring banks to verify their customers' identify and to obtain statements from them about currency and certain negotiable instrument transactions of more than $10,000. The decree gives strong enforcement powers to the National Banking Commission.

- Under current Panamanian law, the Banking Commission has direct oversight over the banks in Panama. Under Cabinet Decree 41, the Banking Commission has the responsibility for ensuring that banks are complying with the requirements of Decree 41 through inspections and examinations. Decree 41 is more expansive in some respects than the present US requirements (e.g. requiring the aggregation of multiple transactions below $10,000 over several days and covering certain transactions involving negotiable instruments).

- On March 19, the Commission issued regulations implementing the currency transaction requirements of Decree 41. These regulations will take effect on May 1, 1990.

  The Decree has the force of law pending legislative action. The GOP is preparing to present it to the National Legislature for immidiate consideration.

Other Law Enforcement Actions:

- The Government of Panama recently took decisive law enforcement action to arrest 4 Colombian nationals using Panama as a transit point to ship narcotics to the United States. The GOP then expelled the fugitives to the US where they are presently being prosecuted on narcotics trafficking charges in the Southern District of Florida.

- The Panamanian police forces made several broad sweeps of locations in and around Panama City believed to be havens for drug pushers and other common criminals. These raids, which resulted in hundreds of arrests, enabled the Panamanian police to re-establish control over these areas.

- The Endara Government has been providing rapid and effective cooperation in the interdiction at sea of Panamanian flag vessels suspected of narcotics trafficking. For example, in January, when the US Coast Guard interdicted a suspicious vessel on the high seas,

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within hours the Endara government confirmed the Panamanian registry of the ship and authorized the USG to take all necessary law enforcement actions against it. When the Cubans challenged the US actions in the United Nations Security Council, the GOP publicly asserted that it had granted the US the authority to act and helped the United States prove that, with Panamanian assistance, it had acted fully in accordance with international law.

- The GOP wants to move rapidly to ratify the 1988 Vienna Narcotic Drugs and Psychotropic Substances Convention because it wants to be one of the first nations to ratify the treaty. Because Panama already has criminalized money laundering and has a strong anti-narcotics law (which was not actively enforced by the Noriega regime), the GOP is in a position to implement the Convention's key provisions rapidly.

Strengthening Governmental Institutions:

- The GOP is moving rapidly to strengthen Executive branch institutions and structures critical to anti-narcotics efforts.

- The GOP has established an antinarcotics committee composed of representatives from concerned Cabinet agencies which meets weekly to develop GOP antinarcotics policy and priorities and examine budgetary requirements.

- The GOP is restructuring its public forces in such a way as to, among other objectives, enhance their effectiveness in anti-narcotics matters. For example, the newly created National Police, under the jurisdiction of the Ministry of Government and Justice, is expected to have traditional "cop on the beat" police responsibilities. The Technical Judicial Police (PTJ), working in close coordination with the Attorney General, will have responsibility for at least some of the GOP's anti-narcotics investigations and operations. Moreover, a special anti-narcotics unit has been provisionally established within the PTJ.

- In order to deter internal governmental corruption and misappropriation of government funds, the GOP has established, by Cabinet Decree No. 36, a Comptroller General's Office, with a special unit dedicated to investigating and auditing governmental functions; the magistrates comprising this unit have the power to adjudicate remedies including ordering restitution of state property wrongfully taken.

Mr. ARONSON. As the letter said, on the one bank that Ford is alleged to have been a member of, he no longer is on the board. He says he is not a part owner.

As the story implied, he held stock options. President Endara is still a member of the board of the bank that was mentioned. Attorney General Cruz is no longer a director of the bank that was mentioned. He was for two years. He says the money-laundering charges were false.

PANAMANIAN BANKING LAWS PREVENTING LAUNDERING

Mr. OBEY. Are you personally satisfied that sufficient changes have been made with respect to Panamanian banking law to assure us that you would not have the trend in the future that was predicted by a U.S. official in that New York Times article?

Mr. ARONSON. What I think is that the recent decision by the cabinet, if it is affirmed by the legislature, is a very good step forward in strengthening their regulatory powers.

Mr. OBEY. When will it be affirmed by the legislature?

Mr. ARONSON. I am not sure. I will find out for you.

[The information follows:]

President Endara has submitted Cabinet Decree 41, requiring the recording of cash bank transactions in excess of $10,000, to the National Assembly for ratification along with a number of other Cabinet Decrees while the Assembly was not in session. The Assembly has not set a date for considering these decrees. However, the Decrees have the full force of law pending Congressional action. In fact, the Panamanian Banking Commission approved the implementing regulations for the Decree on March 19 and they are scheduled to go into effect on May 1, 1990. Our assumption is that the national assembly will address the Endara government's request to ratify the Cabinet decrees in bloc at an early date once they have finished other previous business, such as the adoption of the national budget.

Mr. OBEY. Panamanian banking law is actually not so bad. The real issue is whether they will enforce the statute that they have. Their law was changed a few years ago, but it never was enforced. As I mentioned, I think they strengthened their regulatory powers.

I think the real question is, is this regime committed to rooting out money laundering?

Here is the key paragraph in the article. A senior State Department official says that "existing laws are grossly inadequate" to prevent money laundering and indicates that the U.S. was strongly urging Panama to revise those laws.

Should the Congress indeed move ahead despite the urgent request of the President? Are we acting responsibly if we move ahead before we know that the answer to my last question to you is "yes"?

Mr. ARONSON. Congressman, I think since this new government has been in office, which is two and a half months, they have taken a series of steps, all of which strengthen their capacity to combat money laundering, all of which strengthen our capacity to get information from them to jointly combat money laundering, all of which strengthen their regulatory powers over money laundering, and some of which demonstrate concretely that they are willing to provide us information about Panamanian bank accounts when we have asked for. Finally, they signed a drug cooperation agreement with us pledging to cooperate in money laundering.

All I can tell you is, every test they have been submitted to, they have passed. I think they also are committed to this as individuals. This is anecdotal and it may not satisfy everybody.

Mr. OBEY. What is the content of the legislation which is still pending in Panama?

Mr. ARONSON. I am not sure.

Mr. OBEY. You indicated that Panama is in the process of considering further changes which they have not yet passed.

Mr. ARONSON. No. What I said was that the cabinet has issued a decree that will require all cash transactions or transactions in certain negotiable securities, $10,000 or more, to be reported to the banking commission along with the identity of the customer. That has to be ratified by the legislature.

Mr. OBEY. Yes.

My question is, what——

Mr. ARONSON. When will that happen?

Mr. OBEY. Why is that important and when will it happen?

Mr. ARONSON. Evidently already it has the force of law by cabinet degree. When the administration returns to session, it has to ratify it. It already has the force of law.

Your basic question is a good one. I think they are cooperating. I think they will be very tough on money laundering.

I will repeat again, these three individuals were victims of a regime that was implicated in trafficking. I think their personal integrity has never been questioned. I think they and their cabinet are revolted by the——

Mr. OBEY. I am simply making the point that if we want certain things done to protect the United States' interest, the time to insist on that is before we take action, not afterwards.

I think Congress five years from now will be asked whether or not we asked those questions and whether or not we took the right action based on the answers, so we have no choice but to press on.

TRACKING NICARAGUAN AID DOLLARS

Let me ask you a question with respect to Nicaragua. I am concerned for the same reason several other Members indicated concern. I think Mr. Lehman asked, how do we know this money is going to go where we want it to go?

This request that you are making is ESF. ESF is much tougher to track, frankly, in many instances than development assistance. I will ask again, given the fact this is ESF money you are requesting. How do we in fact provide the meaningful audits that you suggest will be forthcoming, so we can in fact know this money went into the right pockets for the right purposes rather than where it has often gone in that part of the world?

Mr. ARONSON. I will let Mr. Schieck answer that.

Mr. SCHIECK. First of all, just because it is ESF doesn't necessarily mean it is hard to track.

Mr. OBEY. But it often is?

Mr. SCHIECK. It can be. In some of the proposals we have here——

Mr. OBEY. How much of this is not cash?

Mr. **Schieck**. Well, we are proposing a certain amount of this will be projectized assistance. A certain amount would be cash transfers.

In the case of Nicaragua—I am trying to recall the numbers—of the $300 million, roughly $73 million of that would be a cash transfer for balance of payments support.

Consistent with requirements legislated by the Congress, the $73 million would be deposited in a special account and the release of those dollars would have to be in a form which we could track. That is done for all cash transfers around the world, whether it is Nicaragua, Panama or any place.

The remainder of the funds in Nicaragua would support a combination of classical-type projects, where we would have the normal auditing and oversight, and commodity procurements. For instance, with the fertilizer, I would imagine that because of the short lead time, we are going to be doing the procurement ourselves, although a final decision on that has not been made. In essence, AID would be the procurement agency. That means we would disburse directly to the supplier.

In the case of Panama——

Mr. **Aronson**. The funds that will go to clear arrears will also be subject to——

Mr. **Schieck**. That would be direct payments.

In the case of Panama, we still have to work out with the Panamanian government the modalities of how some of this would work. For instance, where we are proposing to channel the $185 million to the private sector, we would have a re-discount fund in the central bank in which banks that had made loans to eligible private businesses would take the paper and go to the central bank and in effect be reimbursed for those loans. That documentation would be available to us to look at to determine the purposes of the loan.

We also would have a procedure to spot check to ensure that the funds lent to the private firms were spent for the purposes intended.

In the case of the arrearages, the $130 million would be a direct payment to the recipient organizations. The $45 million would support classical aid projects.

In summary, we plan to put in place the appropriate accounting procedures and to follow what the Congress has required by implementing the special account procedure when we are doing cash transfers.

USING AID TO PAY ARREARS

Mr. **Obey**. One last question on this. I will put some others in the record. One last question before I turn to refugees.

Concerning the contribution to provide the payments to the IFIs, how many times have we done that before?

Mr. **Fall**. There have been a number of instances of that actually in Central America in which we used some of our resources. In the case of Honduras, 18 months ago it was substantially less than this, but it was in the same cooperative effort and ultimately was successful. Unfortunately, in that case, Honduras immediately fell into arrears again.

We are addressing the problem once more. But that was a problem of Honduras not fulfilling its obligations to the IMF.

Mr. Obey. Should the Congress expect to see this become a routine request on the part of the Administration? Frankly, I am concerned about it.

As I said to the Secretary last week, I think we have an elaborate shell game going on with respect to Third World debt. When you take a look at the routine reschedulings by the Paris Club and you take a look at some of the other problems, we really do not have much debt repayment. We have got many other things to mask the fact that we do not. We are, in fact, shoveling out a great deal of money to countries to meet their own payments to financial institutions. Sooner or later the public is going to say, "Hey, you guys aren't fooling us anymore."

Is this going to become the usual and ordinary practice?

Mr. Fall. I surely don't see it as something that will unwind with great frequency and familiarity before Congress. I think that our effort that has gone into these arrears clearance processes has forced an immense amount of discipline on many of these countries.

We realize that we have got an arrearage problem in quite a number of countries. There are African countries that really confront enormous arrears problems that I think right now the support group process that we have right now to address. But I would foresee that there will be few instances in which a special approach to Congress would be used.

Mr. Obey. Well, let me simply say right here and now that I think if the Congress is going to approve the Administration's request, it ought to be with the understanding that the Administration is going to report on this to the Congress before next year's budget submission. I would like to see the Administration report to us on what they intend to do to deal with the fact that this debt situation is a funny-money game and that we have got to start dealing with it for real.

I just think that maybe we are fooling ourselves, but I do not think we are fooling many other people anymore. This constant reshuffling, this constant pretense that we don't have a very serious uncollectable debt not just in the private sector, but in the public sector, is a very serious problem.

If we are going to engage in honest accounting, we should include that. This is an awful big dishonesty in our calculations right now.

Mr. Fall. It is a point that merits serious, serious review.

I would also say that in the review, in the arrears clearance process, our objective ultimately is to access sizable and substantial lending from these institutions for Panama and Nicaragua over time. I think it is an important undertaking for us in these two countries.

Mr. Obey. I understand. In effect, we are providing indirect appropriations to the international financial institutions, and I don't think that is a healthy thing for us to do.

Mr. Coleman. Will the gentleman yield on that point?

I said I wanted to get into a few more issues a little later. My question is about our involvement in the arrearages. I think you said in your testimony, Mr. Secretary, that it was one-third, and one-third and one-third. That was out of that $130 million, I think. You testified to that mix for that international support for arrearage.

I wondered about why that was fair to the United States, those kind of numbers. I was thinking that the percentage should be more close to our, what we pay in terms of our role in the IMF. Do we have to do that? Do we have to get that kind of money to get the other institutions to provide their thirds.

Mr. **Fall**. Well, Congressman, our thinking in that was that we would establish some proportionality to create the momentum to achieve the objective. That is, that we would expect the Panamanians to contribute a substantial amount.

We looked at the——

Mr. **Obey**. Would you say that again?

Mr. **Fall**. He asked a question specifically about the issue of the sharing of one-third, one-third, one-third regarding the arrears clearance. The point that I was going to make is that we view this as an achievable mechanism to address the arrears clearance. We think that we have asked a substantial participation in this by the Panamanians themselves.

We believe that it is also fair and equitable to foresee this unfolding in an international context. For that reason, we have approached already a number of other countries and have been given clear indications that we have the promise of some measure of solid participation by others in this.

But the objectives to make it proportional, we felt a one-third sharing was probably a good target.

Mr. **Obey**. What happens if you do not get money from other sources? You say you are optimistic now. What if that does not prove to be justified?

Mr. **Fall**. Well, I think that in this particular case, Mr. Chairman, we have every reason to be optimistic. I am not facing failure right now before we launch into this.

Every door that we have opened or indeed had opened for us has shown promise. I might say in that regard that the Japanese have initially come to us with an assurance that they were going to be major players in this. Our approach to others, although not specific at this stage in what funding will be forthcoming, has at least been promising.

I would say that we are not approaching the bridge of failure, but one of success right now.

REFUGEE ASSISTANCE

Mr. **Obey**. I am out of time. Let me switch to refugees.

Your request is for admissions?

Mr. **Lyman**. That is correct.

Mr. **Obey**. What about the assistance programs? The UN High Commissioner for Refugees asked for additional assistance for 1990. Why hasn't the administration requested additional funding for refugee assistance as well as admissions?

Mr. **Lyman**. Mr. Chairman, the $70 million supplemental which will cover our shortfall in admissions allows us to draw on the President's Emergency Refugee and Migration Assistance account for assistance purposes. The President approved a drawdown of $25 million from that account, a large part to the UN High Commissioner.

We will continue to look at urgent requirements. There is a serious budget problem in the international refugee account, and it is the subject of an international effort with the UN High Commissioner to prioritize within his budget and others.

ISRAELI HOUSING GUARANTEES

Mr. **Obey**. I have several other questions on refugees.

Let me ask one other. There is considerable interest, as you know, in having the Congress move forward with a $400 million guarantee for refugees in Israel.

Would the administration have any objection at this point if we simply were to provide authority for up to $400 million in guarantees effective October 1, assuming the same kind of assurances which are usually attendant to the documents for existing assistance is prohibited?

Mr. **Lyman**. The Secretary spoke to this in previous hearings. We are preparing a further statement on it. I am not prepared to answer your specific question today, but we will get back to you with a written response.

Mr. **Obey**. Well, we need one tomorrow.

Mr. **Lyman**. I will try to get it for you tomorrow.

[The information follows:]

We have expressed our support for proposed housing investment guarantees to help resettle Soviet Jews in Israel, provided the United States and Israel can work out satisfactory assurances on the use of the guaranteed funds and issues related to the territories occupied in 1967.

Mr. **Obey**. Anyone else have anything?

Mr. **Aronson**. On that subject?

Mr. **Obey**. On anything.

If not, thank you all very much.

Questions for the Record From Mr. Obey

Submitted to Department of State

Resettlement of Contras

Question. First, to what exent are the Contras returning to Nicaragua with arms, and why are we supporting that by continuing the cash for food program?

Answer. The Resistance, during the last three months, has increased the number of personnel reinfiltrating back into Nicaragua. At present, we estimate that there are 7500 to 9000 Resistance combatants in Nicaragua and between 3500 to 5000 remaining in Honduras. The reinfiltrations continue.

As you know, the Administration has not supported the reinfiltration of additional Resistance forces back into Nicaragua. The cash for food (CFF) program was terminated last month, there will be no further payments.

Question. Give us your overall plan or concept as to how you expect the Contras will demobilize and repatriate? Who will administer the funds requested for this purpose? How and when do you expect the Contras to give up their arms? What do you expect to happen before April 24th?

Answer. With the signing of the Toncontin Accord between the Resistance and UNO on March 23, the demobilization and repatriation process has already begun. The Accord provides for the separation of forces inside Nicaragua, a mutually agreed upon ceasefire verified by UN and OAS observers, secure transitional areas in Nicaragua for the Resistance, the demobilization of all remaining combatants in Honduras to conclude no later than April 20, and the setting up of a UNO/RN commission to resolve demobilization and repatriation problems. We believe that the process will accelerate as soon as reasonable assurances can be given concerning their personal security after demobilization and reentry into Nicaraguan society unarmed.

The initial demobilization of Resistance forces will take place in Honduras. The Yatama forces plan to send a commission, accompanied by CIAV, into Nicaragua to verify that conditions are propitious for them to reintegrate. Yatama forces in Honduras are scheduled to formally demobilize on April 16. The Northern Front forces in Honduras are scheduled for demobilization on April 18. The Southern Front (ERN/S) is also ready to demobilize and reenter Nicaraguan society, but they also require security assurances and have asked that the Sandinistas show good faith by removing MINT and offensive army units from the areas in which they live. The Northern Front (ERN/N) is currently negotiating the location of secure transitional areas through ONUCA and UNO. ERN/N demobilization, as called for in the Toncontin Accord, will take place through the transitional areas and will require somewhat longer to accomplish than the Yatama or ERN/S because of the numbers involved.

The Resistance demobilization and repatriation process should take place and should be relatively rapid once ONUCA and CIAV are fully operational. The major stumbling blocks to Resistance demobilization have been the lack of an established process, and the lack of good faith shown by the Sandinistas who have not lived up to the ceasefire they announced and who have distributed thousands of weapons to their civilian supporters.

As presently written into the authorization, the administration of the funds requested to support Resistance demobilization and repatriation will be through the CIAV, in coordination with the Nicaraguan Government. We have been working closely with the OAS and the UN to make CIAV operational as soon as possible. We have told them that they must start the care and feeding of the Resistance and their families by May 1. We hope they will be ready.

We expect the Resistance to surrender their arms to ONUCA, the organization charged with this responsibility. The actual turning in of arms should begin in Honduras not later than April 20, according to the Toncontin Accords. The arms turn in for the Yatama, and the ERN/S should begin in the near future. The ERN/N will gather in enclaves and the disarmament process will begin from there. We assume that ONUCA will be prepared to receive arms from the Resistance or anyone else inside or outside Nicaragua no later than April 20.

Prior to April 24, the demobilization process and disarming of Resistance combatants in Honduras will have begun. In Nicaragua, once the separation of forces has taken place, and enclaves and an ONUCA-verified cease-fire are established, the ERN/N will begin the demobilization process.

Question. Given the uncertain state of this entire plan why do you expect the Congress will grant you the flexibility you seek for these funds?

Answer. As explained, the Toncontin Accords outlined a demobilization and repatriation agreement between the Resistance and the in-coming UNO government. The just completed Montelimar Summit of the five Central American Presidents called for immediate demobilization "according to the joint plan signed at the Tela Summit . . . and the Toncontin Agreement . . ." Tela called for the UN/OAS International Commission for Support and Verification (CIAV) to handle demobilization, whereas Toncontin mentioned both the CIAV and Cardinal Obando y Bravo to participate.

Flexibility is important to assure the in-coming government of Violeta Chamorro the latitude necessary to meet the demands of Toncontin. Ultimately, it will be the UNO government that bears the effects of any CIAV plan.

Question. The critical element to this scheme is the Contras. They apparently trust no one, not the UN or OAS, not the Sandinistas, and apparently not the U.S. Yet their failure to lay down their arms has jeopardized the prospects for a peaceful transition of power in Nicaragua. What are we—the U.S.—doing to encourage their demobilization? Haven't we in fact encouraged the return of armed units into Nicaragua from Honduras by virtue of our continuation of family assistance payments and the cash for food program through the end of April?

Answer. We agree that the Resistance is a critical element. They have reached agreement with UNO on demobilization mechanisms; they are meeting with CIAV and ONUCA; and they are moving closer to reaching an agreement on traditional areas inside Nicaragua. In fact, the first Resistance force—the Yatama Indian forces—are scheduled to demobilize on April 16, and those Northern Front forces remaining in Honduras will demobilize on April 18.

The U.S. has contributed to the process by providing an initial grant to the CIAV for planning; we are in the process of increasing assistance to CIAV for their operations, which will begin on May 1. Further, we have repeatedly urged the Resistance not to re-infiltrate and instead initiate serious discussions on their reintegration into Nicaraguan civilian life. The Vice-President and the Secretarty of State have, in recent weeks delivered this precise message. Further, we have been working with the UNO transition team in providing technical advice on the mechanical aspects of reaching cease-fire and enclave agreements. And we have in contact with the Sandinistas as well on these issues.

Question. What is the status of the $3.6 million now held in reserve by AID for the UN-OAS resetttlement organization CIAV? Is it the Administration's position that the funds will be withheld from the UN-OAS until the Contras agree to a resettlement plan? If so, why?

Answer. These funds are being distributed to the UN and OAS as called for by the Central American Presidents and the Toncontin Agreement. As it now stands, the UN is responsible for implementation of the demobilization process in Honduras and the repatriation of those demobilized and disarmed Nicaraguans back to Nicaragua; the OAS will handle those Resistance members already inside Nicaragua who need to be demobilized, disarmed and repatriated into Nicaraguan civilian society.

The Administration is not withholding funds from the CIAV until the Resistance agrees to a resettlement plan. The only thing awaiting the disbursement of the funds is agreements with the UN and OAS.

Question. Do you see a role for Cardinal Obando y Bravo in the resettlement plan? If so, what would it be?

Answer. The Cardinal does not yet have a formal role in implementing resettlement. That will be done by CIAV and the UNO government. However, the Cardinal and the Catholic Church will play a significant part through its monitoring network to ensure that returning Resistance combatants and their families are not subject to harassment or intimidation. The Cardinal is to re-establish the Sapoa monitoring network to help ensure that violations of agreements or intimidation are reported promptly to the proper authorities.

Question. $2 million has been requested for the U.S. initial payment for ONUCA. What is the U.S. position on the formation of ONUCA, its size, and its function? Do we favor the formation and development of a large force to disarm the Contras as has been suggested?

Answer. United Nations Observers in Central America (ONUCA), established by the UN Security Council in November 1989 for a period of six months with the possibility of renewal thereafter for an equal period of time, is a peacekeeping operation originally intended and designed to verify the cessation of aid to irregular forces and insurrectionist movements operating in the region and the non-use of the territory of one country by these organizations to attack another. ONUCA's four-phase deployment began in December and should be completed in early May. The original force has 260 military observers, plus air and naval crews, and support personnel.

The United States fully supports the creation of ONUCA. We also supported the UN Secretary General's efforts to expand ONUMCA's mandate to give it a role (1) in demobilizing the Nicaraguan Resistance (RN), (2) in verifying a cease-fire in Nicaragua, and (3) in separating forces inside the country as part of the demobilization process agreed to by the Central American presidents. The first expansion of ONUCA's mission was approved by the Security Council in late March. The second and third elements of the additional mandate were approved on April 20, following the cease-fire agreement reached April 19 in Managua among the Nicaraguan Resistance, the Sandinista authorities, representatives of the Chamorro government, and Cardinal Obando y Bravo.

The United States supported the Security Council's decision on March 27 that expanded ONUCA's mandate to include collecting and securing RN weapons, and approved the deployment of an armed contingent for this purpose. Elements of a Venezuelan airborne infantry battalion already have received weapons from RN forces in Honduras. Beginning on April 25, the entire unit will be involved in the process inside Nicaragua, as will a large percentage of ONUCA's original observer force.

Question. Many of the so called freedom fighters have been "revolutionaries" their entire adult lives. Today they have very little incentive to become farmers as I see it. Many of the leaders of the Contras have no life to return to inside Nicaragua, because they have been fighting the Sandinistas for 10 years. What are we, the U.S.—State Dept., AID or CIA—doing to encourage the Contras to return to a normal life? What are we doing to convince them that being a farmer is more glamorous than being a freedom figher?

Answer. The Resistance has repeatedly said they want to return to civilian life; like other Nicaraguans, they too are tired of war. Under the AID humanitarian assistance program, Resistance members were given civic and vocational training for future reintegration into civil life. Among the most important courses have been literacy, health, hygiene, and sanitation, construction skills (carpentry, cement and adobe type structures), clothing and shoe repair, basic agricultural techniques and human rights training. We have seen that many of the Resistance members are convinced that they will be very successful farmers and want to return to the land after demobilization.

URGENCY OF A.I.D. TO NICARAGUA—

Question. Could the Administration use existing disaster assistance authorities to provide interim assistance to Nicaragua in the event supplemental funds are not available?

Answer. Disaster assistance is designed primarily to respond quickly to natural disasters occurring around the world which threaten human life. Provisions also exist for this aid to be employed in response to a man-made disaster. Nicaragua is a case of urgent need resulting from economic decay and mismanagement. Rapid economic recovery will be key to the survival and stability of this new democracy. While the need is urgent, we do not believe the conditions exist at this time which would constitute a Presidential disaster declaration.

There are however other options which the Administration may choose to exercise, such as the use of contingency authority provided for under Section 451 of the FAA. Under this authority, $10 million in funds could be made available. This would help with immediate needs until the more substantial funds requested in the supplemental assistance legislation is approved.

PANAMA—MONEY LAUNDERING AND BANKS

Question. Based on reported progress to date the Panamanian government is doing the right things and saying the right things, when it comes to bank secrecy laws, tax information exchange agreements, essential chemicals, and maritime law enforcement.

However, as you know, allegations have surfaced in recent news reports about alleged connections between Panamanian government officials and banks alleged to be connected with drug money laundering.

Answer. The Government of Panama has taken steps to preclude a resumption of money laundering in Panama. We are confident that it is doing its best to prevent the international drug cartels from operating in Panama. The bank with which Mr. Cruz was associated, the First Interamerican Bank, is no longer functioning. Mr. Ford has left his position on the board of the Dadeland Bank. President Endara continues on the board of the Banco Interoceanico de Panama and on boards of other institutions.

Question. What assurances can you give the Committee that the Panamanian government will cooperate in the future with the U.S. in drug interdiction efforts and money-laundering investigations?

Answer. The Government of Panama has already demonstrated its interest in preventing Panamanian banks from facilitating or engaging in money-laundering operations and has expanded its cooperation with us on drug interdiction. Its efforts in freezing suspected accounts, its prompt conclusion in January of a cooperation agreement with us, its new decree requiring recording of large cash and negotiable instrument banking transactions, and its request for bilateral disussions with the USG of anti-narcotics agreements all underline Panama's determination to fight illegal drugs. (These discussions are currently underway.) These actions convince us that the Endara administration will do its utmost to cooperate with us on these issues.

PANAMANIAN PUBLIC FORCE

Question. Are there current plans for the Panamanian Public Force? How will it be structured? What has been done to date, and what will U.S. funds be used for?

Answer. The Panamanian Government has decided to convert the former Panama Defense Forces into a civilian police organization, the Panamanian Public Force. The United States with congressional approval, is delivering appropriate assistance to establish a truly professional law enforcement institution, dedicated to providing adequate protection to the citizens of Panama while fully respecting human rights, democracy, and the law. Building on what the United States military has already accomplished under its operational mission to restore public order in Panama, we are providing civilian law enforcement instruction in all areas of basic police skills under the International Criminal Investigative and Training Assistance Program [ICITAP]. We are also providing equipment that is appropriate for police work.

Under the leadership of First Vice President and Minister of Government and Justice Ricardo Arias Calderon and Public Force Commander Eduardo Herrera Hassan, the public force will have primary responsibility for police functions and will be fully accountable to civilian authority under the Minister of Government and Justice. Some security units will be separate from the public force and directly subordinate to other civilian authorities—for example, the technical judicial police is working in close coordination with the Attorney General. The public force budget—in contrast to the PDF budget—is on public record and under control of the executive.

The Government has undertaken a careful screening of candidates for leadership positions in the public force, to prevent placement of Noriega loyalists in positions of authority. Personnel discovered to have been involved in corruption or other criminal activity are being removed from the public force; an Inspector General Corps and an Office of Professional Responsibility are being created. The former PDF numbered about 16,000, the public force is now around 13,000 and is ultimately targeted to be around 10,000. Officer strength has been cut from 1,079 to about 920.

Colonel Herrera Hassan, a highly respected officer in the former Panama Defense Forces, was a rival of Noriega's whom the dictator kept out of the country in a series of diplomatic assignments. Herrera Hassan was removed from his last post as Ambassador to Israel and went into exile in Florida. Named Deputy Commander of the New Public Force, Herrera Hassan moved up when the commander resigned under charges of corruption.

Question. What do you anticipate in the way of future assistance for the public force?

Answer. ICITAP has already made recommendations to the Panamanian Government on general police policy and is assisting in its implementation. ICITAP training contains core tracks emphasizing human rights and due process. Instruction includes training in patrol and traffic supervisory techniques, limited use of force, mechanics of arrest and management courses. In addition, ICITAP is developing a professional training cadre and is working with the GOP to create a new police academy. Technical assistance and training with be provided for investigation of alleged official misconduct, including abuses of human rights. U.S. funds are also being used to purchase uniforms, radios, and limited quantities of civilian police-type weapons; additional funds have been proposed for vehicles. We foresee little or no further U.S. assistance in fiscal year 1991 beyond what the President requested in the second phase of the assistance package. There may be a need for ICITAP funding in fiscal year 1992.

Question. What do you anticipate in the way of aid to the judicial sector?

Answer. The United States has already provided significant technical assistance, training and selected equipment for the Public Ministry and the Supreme Court. This assistance has focused on modernization and professionalization of the court system, including the introduction of new court administrative procedures; provision of law materials and libraries; improved management procedures; judicial training; and merit selection of judges.

The program will continue to stress modernization and professionalization of the Justice Ministry through introduction of improved techniques such as oral proceedings, case tracking and other management information systems, as well as training of prosecutors and other ministry personnel. Attention will be given to developing new skills required by the recent adoption of oral proceeding for certain kinds of cases, as well as the expected incorporation of the technical judicial police into the Ministry. The program would also support the relocation of the Supreme Court and Panama City courts to a new building.

Professionalization of the new civilian police force, subordinate to the Ministry of Government and Justice, is essential. Training and technical assistance will be designed to emphasize community service and human rights, as well as leadership and competent management. Basic police equipment (vehicles, radios, uniforms, laboratory equipment) will be provided.

The assistance program will improve civilian-police relations and strengthen the knowledge and understanding of the role of a civilian government with respect to control of public forces in a democratic government. The program will sponsor consultations from experts, conduct workshops and seminars on these issues, and support publications in Panama. As a complementary program, specially designed human rights courses will be offered to the public forces and governmental officials.

REPAYMENT TO IFI'S

Question. Explain the concept used for the repayment of IFI arrearages from both Panama and Nicaragua.

Answer. Economic reform programs in Nicaragua and Panama must be based on a sound macroeconomic framework and support from the international financial institutions. The traditional means of ensuring sound policies and consistent IFI support is to negotiate a program with the IMF. Likewise, any bilateral assistance, including our own, for the purpose of clearing arrears with the IFI's will depend on the existence of a sound economic program. U.S. assistance for clearing arrears will be part of a multilateral effort.

Question. To date very little has been committed from other donors for Panama. What and when do you anticipate participation from others? What will the Japanese contribute to Panama?

Answer. Other countries quickly demonstrated their support for Panama's democratic government by providing emergency relief. Several of them provided food, medical supplies and other materials to meet Panama's emergency requirements. A few have announced new lines of credits, sent missions to Panama to study the country's needs, agreed to provide technical assistance, and decided to provide some medium term assistance.

We have contacted a number of countries to urge that they provide assistance. Although we are asking that they provide a wide range of support, e.g., through the IFI's and the Paris Club, we are placing special emphasis on setting the foundation for a Panama support group. We hope to convene the support group this summer after we have defined our bilateral program and the GOP has reached an understanding with the IMF. Several governments, including Japan, have indicated a willingness to participate in the support group, but have avoided giving any commitments until they have a clearer idea of our own participation and of the GOP's economic policies. In the interim, the Government of Panama has made direct approaches to Japan and several European countries.

Question. What other donors do we expect to contribute to Nicaragua's arrears?

Answer. While other bilateral donors have reacted enthusiastically to the recent changes in Nicaragua, and have provided some general indications of levels of support they might furnish, they have not provided specific funding and project information. We hope to obtain additional detailed information on other donors' plans during an international donor conference for Nicaragua to be organized by the Government of Italy at the end of May or early June 1990.

Question. Explain what strategy you will use if other donors are not found to repay all outstanding IFI arrearages for both countries?

Answer. Only by clearing their arrears with the IFIs will the governments of Nicaragua and Panama be able to realize significant new inflows of critically needed development resources from those institutions. The arrears clearing process will require several months of close international cooperation with other donor countries and close work with the IFIs themselves. The USG has already contacted other potential donor countries to outline the President's proposed assistance programs and to seek the cooperation of others. Our contacts, necessarily, have been only preliminary as the governments of Panama and Nicaragua have not yet completed their plans for this process and the USG does not yet have resources to participate. We believe that the internationally shared burden of clearing the IFI arrears for both countries which the Administration has outlined to the Congress can be fully implemented.

PANAMA—ENVIRONMENTAL PROJECTS

Question. The Nature Conservancy in cooperation with ANCON, a Panama based environmental organization, have proposed a debt for nature swap in Panama. Essentially $15 million of public funds would be combined with $5 million in private funds to leverage a $100 million debt buyback. The scheme is that the $100 million of Panamanian public debt be purchased in the secondary market, which will be swapped for State bonds with a nominal value equivalent to or below that of the debt. The objective is to create a foundation which will invest the $5 million generated annually from this swap in the protection of watershed of the Canal, the national parks or other protecting areas of Panama. The Nature Conservancy has pledged to raise the $5 million privately.

What is your opinion of this project?

Answer. The Administration recognizes the need to seek creative ways to address environmental problems in Panama. We are eager to examine ways in which the United States can make a meaningful contribution to environmental protection in Panama. We have already begun discussions about using part of the supplemental appropriation to fund technical assistance programs, training and commodity support programs to: (A) protect the Panama canal watershed, and (B) increase the effectiveness and coverage of entities that protect vital natural resources.

Under the immediate action program approved by Congress on February 7, 1990, A.I.D. is providing a grant of $271,000 to the Panamanian National Association for the Conservation of Nature, ANCON, for job creation and conservation works in two national parks in the endangered Panama canal watershed.

Question. Would you or the Panamaian government support this project?

Answer. We are prepared, as part of the detailed analytical and design exercise for a new environment activity, to explore the feasibility of a debt-for-nature mechanism to support parks and natural resources management programs. We are not in a position to judge the merits of this specific proposal without knowing more about it, and without knowing the level of funding that Congress will make available to us for use in Panama. We have indicated our willingness to allot significant amounts of money for this type of project.

MIGRATION AND REFUGEE ASSISTANCE ADMISSIONS REQUEST

Question. The fiscal year 1990 supplemental includes $70 million for additional funding for refugee admissions for 1990. Last summer we provided $85 million in supplemental funds for refugee admissions—why are you having so much difficulty in requesting adequate funds to support refugee admissions?

Answer. The FY 1989 Dire Emergency Supplemental was intended to fund the admission of additional Soviet and Eastern European refugees provided for in Presidential Determination No. 89-15 of June 9, 1989, raising the funded numbers from 90,000 to 112,500. Of these no-year funds, approximately $21 million was not obligated in FY 1989 and remained available to be applied to the FY 1990 program costs.

In September 1989, in testimony before the Judiciary Committees, the Administration stated that the President's proposal to increase the planned FY 1990 admissions from 84,000 to 111,000 funded numbers would require approximately $58 million above the Administration's FY 1990 budget request. This estimate—which was subsequently revised to $70 million in light of higher actual refugee flows through Vienna and Rome—already included the $21 million carried forward from the FY 1989 supplemental.

Question. What is the breakdown between admissions for Soviet/Eastern Europe and for other areas?

Answer. The FY 1990 regional refugee admissions ceilings are as follows: Soviet Union ,50,000 (of which 10,000 are unfunded); Eastern Europe, 6,500; Latin America and the Caribbean, 3,500; Africa, 3,000; The Near East, 6,500; Southeast Asia, 26,500 (Order Departure), 25,000 (First Asylum).

Question. Most of the funding that has been requested will support Soviet Refugees that are now or have been in Rome awaiting processing to come to the United States. How many refugees have been processed through Rome to the United States since the beginning of this fiscal year—and what has been the cost?

Answer. As of the end of March, about 35,500 Soviet refugees came to the United States via the Vienna/Rome route. While we will not know the actual costs related to this caseload for several months yet, our budget estimated that some $81 million would be required for processing (including care and maintenance), transportation and initial resettlement.

Question. How many more refugees, and the associated costs, are projected to come through Rome through the end of the fiscal year?

Answer. At the end of March, there were 9,500 refugee applicants in Rome in various stages of processing all of whom should depart for the United States by the end of May. The budget estimate for this group is some $21 million.

Question. If there is a ceiling of 50,000 for Soviet/Eastern refugees for this year and 40,000 of these slots will be used by refugees coming from Rome, how many actual new refugees will be brought from the Soviet Union?

Answer. The refugee admissions ceiling for the Soviet Union alone is 50,000. The separate admissions ceiling for Eastern Europe is 6,500. We expect to admit approximately 45,000 Soviets from Rome. We expect to admit another 3,000 Soviet refugees directly from Moscow. If private sector funding is forthcoming, an additional 2,000 refugees could be admitted directly from Moscow.

Question. Under the new procedure of processing refugees directly from Moscow how many Soviets have applied for admission to the United States?

Answer. The Washington Processing Center (WPC) has received about 200,000 applications since October 1. Application information for some 80,000 individuals has been entered into the WPC data base.

Question. If only about 10,000 refugees will be processed out of the Soviet Union for this year is there any consideration to increasing the 50,000 ceiling for fiscal year 1990?

Answer. We believe that 50,000 refugee admissions are adequate for the number of Soviet refugees we are able to process during FY 1990. We expect to admit another 10,000–20,000 Soviet emigrants through parole and regular immigration.

Question. The direct processing program from Moscow is supposed to dramatically reduce the per refugee cost—since there will be no housing and transportation costs in Rome. What are the cost savings per refugee?

Answer. With the elimination of the Vienna/Rome pipeline, costs related to the processing of refugees in these two European capitals as well as the costs related to their stay (care and maintenance) while they await admission to the United States are eliminated. In FY 1991, the admissions budget is based on a projection of 40,000 USG funded admissions from Moscow. Projected costs for processing are significantly reduced from the FY 1990 level, and there is no requirement for care and maintenance funds now that Soviet refugees will be processed in and travel directly from Moscow to the United States.

The FY 1991 admissions budget reflects a cost reduction of about $46.7 million from the FY 1990 level. This reduction is primarily in processing/care and maintenance requirements, although there is an increase in transportation costs for Soviets now departing from Moscow.

Question. Will these cost savings effect FY 1990 and enable a reduction in the $70 million request?

Answer. There are no cost savings anticipated in FY 1990 that will enable a reduction in the $70 million supplemental request for refugee admissions. The request reflects our current best estimates of costs.

The supplemental appropriation of $70 million, when added to our current availabilities, should adequately fund our admissions requirements in FY 1990 which include closing down the Vienna/Rome route.

REFUGEE ASSISTANCE FUNDING

Question. The UN High Commissioner for Refugees has called for additional assistance contributions from countries to meet refugee needs for fiscal 1990. Also, the International Red Cross has received a decrease in U.S. funding for FY 1990 and has asked for an increase in assistance. Why haven't you requested funding for assistance in your supplemental?

Answer. The Administration's request for a supplemental appropriation in the amount of $70 million to cover additional refugee admissions requirements would permit the use of the Emergency Refugee and Migration Assistance Fund to address urgent refugee assistance requirements.

We began FY 1990 with a balance of just under $50 million in the Emergency Fund. To date, the President has authorized the use of almost $25 million to address urgent assistance needs. Of this amount, $22.45 million will go to the UN High Commissioner for Refugees and $1.3 million will go to the International Committee for the Red Cross.

There remains a balance of some $25 million in the Emergency Fund to address future needs. With the enactment of a $70 million supplemental appropriation for admissions, we could expect to address urgent assistance needs by drawing on this balance.

Question. What is your estimate of the minimum needed to provide assistance to the United Nations and to the International Red Cross for refugee assistance in fiscal year 1990?

Answer. There is no complete answer to the question of the minimum needed. Much depends on the ever changing situation on the ground and on the actions of other donors. With funds appropriated under the Migration and Refugee Assistance Account for FY 1990, the U.S. will continue to be the single largest donor country, and we are constantly working to promote greater contributions from others. Nevertheless, it is a fact that U.S. contributions from MRA have been reduced by earmarks which divert funds from our request for the UNHCR and ICRC programs for other purposes.

The Emergency Refugee and Migration Assistance (ERMA) account is needed to address the new emergencies (e.g. Liberians in Guinea and Cote d' Ivoire) and opportunities (e.g., ICRC assistance in Panama). To date, half of the $50 million ERMA account has already been drawn down.

Enactment of a supplemental appropriation for refugee admissions programs will ensure the availability of the ERMA Fund for urgent assistance needs. If funds identified under the MRA account and those in the ERMA are available for assistance purposes, we believe a U.S. fair share of the international needs will be met.

Question. Last year Congress provided $40 million above the Administration request for additional funding for the Emergency Refugee account. It is my understanding that the President is authorizing the drawdown of approximately $25 million from the emergency fund to meet additional assistance requirements. When will Congress be notified of this drawdown? What will be the remaining balance in the emergency fund once this draw down has taken place?

Answer. On March 7, the President authorized the use of $24,950,000 of the $49,829,000 available in FY 1990 from the Emergency Fund as follows: $10 million for United Nations High Commissioner for Refugees (UNHCR) for further impelementation of the Comprehensive Plan of Action; $12.45 million to UNHCR for its programs in Africa ($5.25 million for emergency programs in the Horn, $1 million in Angola and Zaire, $1.2 million on behalf of refugees from Liberia, and $5 million for life-support programs in Malawi); $2 million to the International Committee of the Red Cross (ICRC) for its programs in the Horn of Africa; $200,000 to the League of Red Cross and Red Crescent Societies (League) for its programs on behalf of Liberian refugees; and $300,000 to ICRC for its protection, medical and relief programs in El Salvador and Panama.

Letters notifying the Congress of this drawdown were sent by the Department on March 20, 1990.

There is currently a balance of $24,879,000 remaining the Emergency Fund.

Question. Why haven't you drawn down enough funding from the emergency account to meet the requests of the UN High Commissioner? What unmet needs are there to support the International Red Cross?

Answer. We began FY 1990 with a balance of just under $50 million in the Emergency Refugee and Migration Assistance (ERMA) Fund. To date, the President has authorized the use of almost $25 million of the funds available to address urgent assistance needs. Of this initial drawdown, $22.45 million will be contributed to the UN High Commissioner for Refugees (UNHCR). The United States continues to be the largest single donor to UNHCR.

The first ERMA drawdown in FY 1990 included $2.3 million for operations of the International Committee of the Red Cross (ICRC) in Panama, El Salvador, and the Horn of Africa. Responses to ICRC needs are considered in the context of all humanitarian requirements. In the meantime, ICRC is implementing its programs where access to conflict victims and political prisoners is possible.

There currently remains a balance of some $25 million in the Emergency Fund to address future needs. With the enactment of a $70 million supplemental appropriation for admissions, we could expect to address urgent assistance needs by drawing on this balance.

DOMESTIC REFUGEE ASSISTANCE

Question. Last year there was an imbalance between funding for refugee admissions in our bill and the domestic resettlement program (Refugee Entrant Assistance) funded under the HHS bill. We closed that difference by providing $15 million in the Foreign Assistance bill for Refugee Entrant Assistance. Will the additional $70 million requested in the Foreign Assistance supplemental result in another imbalance? What funding is available in FY 1990 under the Refugee Entrant Account?

Answer. Following meetings with State and local government officials, voluntary agencies, and refugee leaders, the annual consultations with the Congress on refugee admissions for FY 1990 took place in September, 1989. After considering Congressional views, the President set a ceiling of 111,000 funded refugee admissions. This was a substantial increase from the 84,000 admissions for which the State Department requested and received funding. Therefore, a $70 million supplemental appropriation is needed by the State Department to fund the increase in admissions.

According to the Office of the U.S. Coordinator for Refugee Affairs, under the Refugee Entrant Account, $384 million is available in FY 1990. This amount includes a Congressionally-mandated $15 million transfer of funds from the State Department to HHS. The Office of Refugee Resettlement (ORR) at HHS has established certain funding priorities to ensure that high priority programs are run effectively.

FUNDING FOR UNRWA

Question. Last year the Department of State allocated a total of $63 million for UNRWA, which provides assistance to refugees in the West Bank and Gaza. In the allocation process this year UNRWA has been allocated only $50 million—which is more than a 20 percent reduction in funding. Based on the problems on the West Bank and Gaza why has there been a reduction in funding for UNRWA?

Answer. Reduced U.S. contributions to international humanitarian and refugee organizations in FY 1990, including UNRWA, reflect the impact of earmarks diverting the funds requested for these organizations for other purposes. A U.S. contribution to UNRWA at the $50 million level, while a reduction from last years level, still makes us the single largest donor to that organization. This reduced contribution, however, does not indicate any lessening of support for UNRWA's work or dissatisfaction with the agency. The U.S. is committed to UNRWA's programs which makes a significant contribution to U.S. political and humanitarian goals in the region. For FY 1991, we have requested $63.3 million for UNRWA.

Question. Are there plans to use funding under the Emergency Fund to make up for some of the deficit?

Answer. Regarding the second part of the question, we are actively reviewing the option of seeking funds from the Emergency Refugee and Migration Assistance Fund (ERMA) to address urgent needs of the Palestinian refugees.

REFUGEES RESETTLING IN ISRAEL

This year's bill includes $25 million for Soviet, Eastern European and other refugees resettling in Israel. That funding was provided prior to the recent upsurge in refugees coming to Israel. If current refugee levels hold for the year there will be about 75,000 refugees from the Soviet Union this year compared to 6,000 last year.

Question. Answer. What are your projections for the number of refugees resettling in Israel?

Answer. Since the beginning of FY 1990 (October 1, 1989) through February 1990, the Jewish Agency for Israel reports that 20,228 persons from "countries of distress" have immigrated to Israel. Of these, 17,622 are from the Soviet Union, 720 from Eastern Europe and the remaining 1,886 are from Asia and Africa.

In January, 5,572 refugees arrived in Israel. In February a total of 6,114 refugees arrived (5,703 from the Soviet Union, 156 from Eastern Europe and 255 from Asia and Africa). If this trend holds for the next ten months of CY 1990, total refugee arrivals in Israel could reach approximately 67,000 persons. (This figure is arrived at by taking January arrivals and multiplying by 10 the 6,114 February arrivals for a total of 66,710). However, there could be significant increases or decreases in any of the groups, particularly those coming from the Soviet Union. These total figures represent only one way of making an estimate.

Question. Does State have any plans to increase the amount of funds provided under the Soviet/Eastern European resettlement assistance for Israel?

Answer. The U.S. grant represents only a small portion of the funds needed for refugee resettlement in Israel. The UIA in 1989 contributed $304 million toward the Jewish Agency's $414 million budget. World Jewry is currently seeking $600 million over the next three years to help with costs of absorbing Soviet immigrants. For these reasons, we believe that current grant level is appropriate contribution from the U.S. Government.

HOUSING GUARANTEES FOR ISRAEL

Question. The Government of Israel has requested $400 million in housing loan guarantees to support the increase of Soviet refugees coming to Israel. Do you feel that this request is in line with the number of refugees now projected to settle in Israel?

Answer. The $400 million is the level that the Israelis have discussed, based on their projections of refugee arrivals in Israel. The Administration supports the program provided the United States and Israel can work out satisfactory assurances.

The Housing Guaranty Program is administered by the Agency for International Development (AID). I refer further questions to those in AID responsible for the program.

Questions for the Record From Mr. McHugh

SUBMITTED TO DEPARTMENT OF STATE

CONTRA DEMOBILIZATION

Question. Could you describe as specifically as possible your plans for demobilizing the Contras?

Answer. With the signing of the Toncontin Accords between the Resistance and UNO, the demobilization and repatriation process are underway. On April 16 and 18, RN forces in Honduras will formally demobilize and disarm. For those forces inside Nicaragua, agreement on transitional areas (enclaves) is proceeding. The CIAV and ONUCA are putting their operations into place. All this as outlined in the Toncontin and Montelimar Agreements.

The U.S. supports the agreements of the Central American Presidents and the Toncontin Accord between UNO and the RN. Our assistance request to Congress is built on this regionally-devised structure. We are committed to seeing the full implementation of those agreements on demobilization. We believe that a good start has been made, by all parties, to make the process work. The key now is to see that the process remains on track.

Question. Your request for Nicaragua includes $32 million for the purpose of demobilizing and repatriating the Contras. How did you arrive at this figure?

Answer. This figure was based on an estimate that there will be approximately 15,000 Resistance combatants and 45,000 family members who will be involved in the whole demobilization and repatriation process. We believe that the figure is adequate to provide for immediate resettlement needs and some start up incentives once they are back in Nicaragua. The fundamental purpose of the assistance is to give them the means to become self-sustaining members of the Nicaraguan community rather than a burden on the new government.

Question. Would the Administration oppose a provision in the bill stipulating that no assistance should be provided to any member of the Contras unless he or she turns in any weapons they may possess? If so, why?

Answer. The Administration would oppose such a blanket ban because it does not take into account the recently signed Toncontin Accords, and because it is likely to hinder rather than help the process of prompt demobilization. The Toncontin Accords contain a provision for transitional areas for Resistance members in Nicaragua. The Resistance will enter these encalves armed and be demobilized as conditions are created to assure their security. Neither the Toncontin nor the just-completed Montelimar Agreement precludes assistance to armed Resistance members in security zones. The point we have stressed is the importance of a step-by-step approach of confidence-building in the demobilization process. Without an assurance of assistance to Resistance members inside Nicaragua during the demobilization process, the Resistance would be less likely to enter security zones and the risk of levels of violence is increased as RN members seek ways to acquire food, medicines, etc. For these reasons, we would oppose such a provision in the bill.

NICARAGUA IFI ARREARS

Question. Your proposal includes a request to provide $50 million to help Nicaragua repy its arrears to the international financial institutions. But my understanding is that Nicaragua currently owes the World Bank $172.7 million and the Inter-American Development Bank an additional $56.8 million, a total of $229.5 million. I also understand that by the end of this year the amount Nicaragua owes to these institutions will be closer to $300 million. Where do you expect the balance of the funds to come from to help Nicaragua pay off its arrears? Have you had any discussions with other bilateral donors about this issue to date and what kind of response, if any, have you received? Have any countries pledged a specific amount for this purpose? If so, which countries and how much?

Answer. Only by clearing their arrears with the IFIs will the governments of Nicaragua and Panama be able to realize significant new inflows of critically needed development resources from those institutions. The arrears clearing process will require several months of close international cooperation with other donor countries and close work with the IFIs themselves. The USG has already contacted other potential donor countries to outline the President's proposed assistance programs and to seek the cooperation of others. Our contacts, necessarily, have been only preliminary as the governments of Panama and Nicaragua have not yet completed their plans for this process and the USG does not yet have resources to participate. We believe that the internationally shared burden of clearing the IFI arrears for both countries which the Administration has outlined to the Congress can be fully implemented.

While other bilateral donors have reacted enthusiastically to recent events in Nicaragua, and have provided some general indications of levels of support they might furnish, they have not developed their plans in detail. We hope to gain further precision on donor plans during the international donor conference for Nicaragua to be organized by the Italian government at the end of May or beginning of June.

Question. Even assuming you are able to put together a package to clear the immediate arrears, when would you expect the flow of assistance from these institutions to Nicaragua to be positive?

Answer. Once the new government is able to clear arrears with the International Financial Institutions, they could expect to receive $40 to $45 million under an IMF standby arrangement. The last IMF standby program was in 1979 for about $44 million. Since there are no arrears to the IMF, the net IMF transfers to Nicaragua would be strongly positive. Because the Nicaraguan programs for the World Bank and the Inter-American Development Bank [IDB] have been suspended for some time, it will take time to redesign and develop loan proposals. Therefore, it is very difficult to estimate how much in new loans will be available in 1990 and 1991. If a strong enough economic framework is developed, substantial fast-disbursing resources could be provided by both the World Bank and the IDB.

NICARAGUA TRANSPORTATION SECTOR

Question. What priority does the in-coming government assign to the transportation sector?

Answer. The UNO economic plan addresses rehabilitating transportation services as a component of rebuilding the infrastructure. The plan indicates that transportation routes and equipment, previously State-operated, will be auctioned to private enterprises and cooperatives. Our conversations to date with the UNO economic team have focused on essential inputs to reactivate agriculture and industrial production. We expect balance of payments support will go for the import of such goods as fertilizer, farm equipment, capital equipment and raw materials. Transportation infrastructure, also a critical element in restoring normal economic activity, is an area that may require further assistance.

Question. I am told that the UNO agenda for economic recovery mentions rehabilitating the bus transport sector specifically. Is that correct? If so, did the Nicaraguan economic team ask directly for assistance in this area?

Answer. To date, UNO economic advisors have not specifically identified assistance to the bus transport sector as among Nicaragua's most urgent aid requirements. In the context of this first appropriation, it is unlikely that funds would be used directly for the bus transport sector. However, we will be examining this question in more detail. It is our understanding that the new government intends to encourage private enterprise and cooperatives to be the key element in rehabilitation of the transportation system.

Question. Your proposal contains $73 million for "private sector production imports" for equipment, spare parts, raw materials, and intermediate goods to rehabilitate existing industrial and agricultural facilities. Do you plan to allocate any of this money to the transport sector? If not, why not?

Answer. The private sector has been decimated by the practices and policies of the Sandinista government. There is a critical need for capital equipment, replacement parts and productive inputs such as raw materials and intermediate goods. The $73 million will provide foreign exchange which the private sector can draw upon in exchange for local currency. Given the long period that the private sector has been without the means to acquire capital goods we anticipate that the $73 million will be utilized in a short period of time. Foreign exchange priorities will be set by the Chamorro Government according to its development and economic agenda in consultation with A.I.D. After the Chamorro Government takes power on April 25th and it begins implementing its economic program, other needs may arise.

Nicaragua Aid

Question. Realistically, do we expect the $500 million you are requesting for this year and next year to do the job? Or are we going to have to be in Nicaragua for along time? What is your dollar estimate of Nicaragua's overall, short-term, requirements, and the percentage of the total the United States expects to provide under the request before us? What is your best estimate of long-term financing requirements?

Answer. The $300 million we are requesting this year is essential immediate assistance for putting Nicaragua's economy back on track after years of economic deterioration. Even as it recovers, however, Nicaragua is a developing economy for which a continuing U.S. economic assistance program will be appropriate. Some of the $300 million requested for 1990 and a more substantial portion of the $200 million requested for 1991 will be devoted to beginning an ongoing development assistance program for Nicaragua to alleviate poverty and spur longer term growth and development.

For the short term, UNO economic advisors have estimated that $500 to $600 million per year in economic assistance will be needed over the next three years. We agree that the needs are great for rehabilitating and restructuring the economy. In the long term, economic assistance will be determined in accordance with Nicaragua's economic development needs and priorities and appropirate U.S. contribution, along with assistance from other donors, especially the International Financial Institutions.

Question. What have other donors pledged for the short-term and the long-term?

Answer. The bilateral donor community has reacted very positively to the results of Nicaragua's election and to the political and economic change now in store for that country. A number of countries have provided preliminary indications of aid levels; initial information shows that the European Community, the U.K., Germany, Spain, Italy, Denmark, Norway, Sweden, Austria, Switzerland, Canada and Japan are planning at present to provide a total of over $300 million.

The Italian government is planning to host an international donor pledging conference for Nicaragua May 31–June 1. The United States will attend this conference, at which time we will likely have a clearer idea of total aid levels.

Question. What will the $200 million you are seeking for fiscal year 1991 be used for and how does that relate to the assistance you are seeking in the current fiscal year?

Answer. We estimate that balance of payments support will remain critical to the recovery of Nicaragua's economy and private sector into 1991. We also intend for development assistance to consolidate the formation of a U.S. economic development program that will address needs in such priority areas as health, education, democratization, agriculture and rural development. The FY 1991 assistance will follow programs and priorities set in FY 1990 and aimed to continue U.S. support as the Chamorro Government works to implement the economic recovery plan.

Question. Without prejudicing the specifics of the overall request, what are the one or two most important areas requiring attention which could threaten Mrs. Chamorro's first 100 days in office if not supported sufficiently? What sector(s) deserve the most attention over the longer haul?

Answer. The administration has designed the aid package to meet Nicaragua's most pressing immediate needs. Stability and rapid economic recovery will depend on the availability of foreign exchange to purchase critical agricultural inputs for the planting season and to finance essential private sector inputs. Assuring supplies of petroleum and petroleum products is vital to supporting economic activity and the stability of the New Chamorro Government. Finally, contributing to the clearing of arrears to the International Financial Institutions is key to normalizing relations and paving the way resumption of resource flows from these institutions.

Over the longer term, assistance to continued private sector development, and to meeting needs in such sectors as health, education, and rural development will be a primary focus of attention.

Question. Do you expect Nicaraguans living outside the country to return and to bring back their capital? If so, is there any evidence to suggest that is happening at this time?

Answer. Nicaraguans abroad have expressed great interest in returning home to live, work and invest. A group of 80 Nicaraguan businessmen from Miami traveled to Nicaragua in mid-March to explore investment opportunities. In late March Vice President-elect Virgilio Godoy addressed 1,500 Nicaraguans in Miami about the new government's support for private enterprise. (Two weeks earlier, well over 1,000 Nicaraguans attended a Miami speech by Chamorro's top economic advisor, Francisco Mayorga.) Many Nicaraguan businessmen have indicated that while they would like to return home, they need first to evaluate the new government's implementation of its economic program—to see if the climate is propitious for new investment. Such investment will be crucial for the new government, and it is important that we help Mrs. Chamorro establish confidence in economic prospects in Nicaragua, to encourage the return of businessmen and capital.

Question. Does the Administration have plans that could facilitate the return or entry of American firms to Nicaragua to strengthen its return to a market economy?

Answer. The U.S. private sector can play a very important role in the recovery of the Nicaraguan economy. We believe that the Nicaraguan economic recovery period should offer a variety of trading and investment opportunities for U.S. firms. A return of democracy and stability to Nicaragua will greatly boost U.S. business confidence. The Commerce Department is examining ways to implement commercial programs and has initiated a business outreach program aimed at encouraging U.S. businesses to become involved in Nicaragua. OPIC has an existing, but dormant, bilateral agreement with Nicaragua which would allow operations as soon as a waiver for OPIC operations is approved or GSP is restored. OPIC is already making preparations for an investment mission in the near future.

PANAMA PRIVATE SECTOR

Question. $185 million of the $500 million you are requesting for Panama is designated to revitalize the private sector. What specifically will that money be used for?

Answer. The private sector, which can serve as an engine of economic growth, requires financing for badly-needed investments. The grant of $185 million would be used to open a special line of credit through the banking system to finance private sector business investments. Since the program will be demand-driven, we cannot specify exactly how the funds will be used. However, our discussions with the Government of Panama and with the private sector indicate that this grant would most likely be drawn down for investment in the construction, tourism, commercial and agricultural sectors. The criteria for approving loans will include rapid and effective use of funds, job creation, and export generation. As loans are repaid to the GOP, the funds will be made available for GOP development projects.

Question. What is the current situation with respect to private sector investment? Is flight capital returning? If not, why not? If so, to what degree?

Answer. The private sector has responded positively to recent developments, showing an increased confidence in the country's future. Our information is more anecdotal than comprehensive or systematic, but it suggests that investment is increasing. For example, it is estimated that more than 50 percent of the businesses that had been closed by the December looting have reopened. In addition, we have already received sufficient business applications to use all of the money made available in the first phase of the assistance package. Similarly, we understand that flight capital has begun to return, as indicated by the rise in bank deposits. However, we do not have reliable, detailed data on flight capital flows.

PANAMA IFI ARREARS

Question. As with Nicaragua, a portion of your request ($130 million) is to help the new government clear its arrears with the international financial institutions. Has the United States government ever assisted any other government in clearing arrears with these institutions? If so, which governments?

Answer. The United States helped the government of Honduras clear its arrears to the international financial institutions in 1987. Unfortunately, Honduras did not follow through with a strong economic adjustment program and subsequently fell back into arrears. We have been asked to participate this year in a financial package that will help the new government of Honduras resolve its arrears problem.

We are helping the governments of Panama and Guyana resolve their arrears problems through an approach referred to as "intensified collaboration," introduced by the IMF in the fall of 1988. The strategy helps countries ineligible to use IMF resources due to the presence of arrears to normalize financial relations. Typically, a country with arrears is also a country that has rejected economic reforms. Normalizing relations involves implementing a comprehensive and credible economic reform program that can merit the support of the international community and provide the basis for mobilizing resources to clear arrears.

Key to the strategy's success is the establishment of support groups of friendly donor countries that are willing to provide the financing needed to assist the country's adjustment efforts and to clear arrears. The United States has agreed to lead a support group for Panama. A support group exists for Guyana, under the leadership of Canada. The United States has committed $1 million in economic support funds [ESF] to Guyana's support group to help clear arrears to the IMF, World Bank, and Caribbean Development Bank. A support group was formed for Somalia under Italian leadership, but donors have withheld assistance due to human rights problems in the country.

We will be helping the Government of Nicaragua clear its arrears to the World Bank and the IDB in the context of an international effort. Nicaragua does not have arrears to the IMF. Like Panama, Guyana and Honduras, Nicaragua needs an IMF-supported comprehensive economic reform program as the basis for mobilizing resources to clear arrears. A strong economic program will establish the supportive macroeconomic environment needed for the World Bank and IDB to resume significant lending operations. The proposed U.S. contribution of $50 million to clear arrears will help catalyze international donor support for this important effort. We expect the World Bank to play in important role in coordinating donor support.

Question. Could you provide for the record the amount of arrears owed by any other governments to any of the international financial institutions in which we participate (as of this date), and a statement as to whether we plan to help any of those governments to clear their arrears?

Answer. If countries are to achieve market-oriented growth, consistent with our political and economic values, they will need to work with the Internatioanl Finanical Institutions [IFI's] in implementing comprehensive macroeconomic and structural reforms. Thus, it is important that we be prepared, if necessary, to work with the IFI's and these countries to encourage appropriate economic management. Countries with arrears to the IFI's are generally unable to receive support from those institutions.

Decisions on whether and how best to help arrears countries repay their overdue obligations to the IFI's will necessarily be made on a case-by-case basis. U.S. consideration will depend on a number of concerns, including overall assistance levels, policy priorities, and the pace of reform in a given arrears country. By helping a country clear its arrears, the United States reduces potential future requests for bilateral assistance and contributes to a strengthening of the financial position of the IFI's. Given the IFI's central role in addressing economic reforms, U.S. interests are well-served by working with these institutions.

The following tables indicate country arrears (in millions) to the international financial institutions in which we participate:

International Monetary Fund [IMF]

[Countries with overdue obligations of 6 months or more as of March 29, 1990]

Guyana	136
Honduras	34
Campuchea	48
Liberia	401
Panama	251
Peru	826
Sierra Leone	91
Somalia	134
Sudan	1,165
Vietnam	133
Zambia	1,050

International Bank for Reconstruction and Development [IBRD]

[Countries in non-accrual status (arrears of 6 months or more) as of April 3, 1990]

Guyana	48
Honduras	123
Liberia	81
Nicaragua	175
Panama	201
Peru	700
Sierra Leone	5
Syrian Arab Republic	240
Zambia	233

Inter-American Development Bank [IDB]

[Countries in non-accrual status (arrears of 6 months of more]

Honduras	47
Nicaragua	59
Panama	162
Peru	232

Asian Development Bank [ADB]

As of February 21, 1990, three countries had arrears to the ADB of at least 30 days, but no country was in non-accrual status (i.e., arrears of 1 year or more). Countries with arrears of at least 30 days are Afghanistan ($.18 million), Kampuchea ($1.7 million), and Vietnam ($5.6 million).

African Development Bank [AFDB]

[Countries in non-accrual status (arrears of one year or more) as of December 31, 1989]

Comoros	7
Equitorial Guinea	1
Liberia	53
Sierra Leone	2

Question. You have indicated that, even with our assistance, the IFIs will be taking more out of Panama than they put in 1990 and 1991. How do we know that the new Panamanian government has the will and/or the resources to make these payments?

Answer. The Government of Panama has taken steps which, if supported by the international community, will permit the country to become current in its obligations to the IFIs. It has already reserved the dollars necessary for it to make a $130 million contribution to clearing its arrears. In addition, President Endara's 1990 budget submission to the Panamanian Congress provides for payment of the maturities falling due this year. The Congress is expected to approve the budget proposal.

The Government of Panama will have a strong incentive to keep current with the IFIs. Although net flows from the IFIs will be negative this year, we expect they will be heavily positive in 1991. Moreover, Panama's good relations with the IFIs will substantially improve its international image and open the door to significant amounts of capital from other sources.

Question. What other donors have agreed to help clear Panama's arrears? How much have they offered to put up?

Answer. We have contacted a number of countries to urge that they provide assistance. Although we are asking that they provide a wide range of support, e.g., though the IFIs and the Paris Club, we are placing special emphasis on setting the foundation for a Panama support group. We hope to convene the support group this summar after we have set in motion our bilateral program and the GOP has reached an understanding with the IMF. Several governments have indicated a willingness to participate in the support group, but are unwilling to specify their commitments until they have a clearer idea of our own participation and of the GOP's economic policies. We are confident that the international community will respond with adequate support.

PANAMANIAN MILITARY

Question. The old PDF (Panama Defense Force) was a brutal and corrupt military force that showed little regard for democracy or basic human rights. What assurances can we provide to our colleagues that the Panamanian military will not simply take over the country once again in the future and revert to its old ways?

Answer. The new security organization will be primarily responsible for police functions and fully accountable to civilian authority under the Minister of Government and Justice, or other elements of the Government of Panama such as the attorney general, as in the case of the technical judicial police. The Endara administration will ask Congress to make the appropriate changes to Panamanian law.

The Government has undertaken a careful screening of candidates for leadership positions in the new Panamanian Public Force (PPF) in an effort to prevent placement of Noriega loyalists in key positions of authority. Personnel discovered to have been involved in corruption and other forms of criminal activity are also being removed from the PPF. This is a sensitive and challenging task that will contiue as more incriminating information comes to light but, in discussions with us, Panamanian officials have stressed that this matter is a top priority for the new government.

The Government of Panama has dispersed some of the power and authority that had previously been held by the PDF. For example, separate entities, subject to civilian supervision, have been formed to handle the criminal investigation penal system, immigration, customs, anti-narcotic enforcement and maritime and air services formerly performed by the PDF. This new structure has added greater institutional checks and balances against any possible military attempt to take control of the country.

Under the leadership of Vice President and Minister of Justice Arias Calderon and PPF Commander Herrera Hassan, an Inspector General Corps (IG) is being created, along with an office of professional responsibility which will work with the IG.

U.S. administration of Justice/ICITAP training contains core tracks emphasizing human rights and due process.

Question. How much military and/or police funding do you expect to provide under this assistance package? Please be as specific as possible as to how these funds will be used.

Answer. The supplemental will fund the continuation through FY 1991 of training and technical assistance activities initiated by the International Criminal Investigative Training Assistance Program (ICITAP) under the emergency assistance package with the Panamanian National Police and the Technical Judiciary Police. Civilian police experts from around the country will be participating in ICITAP activities.

ICITAP has made recommendations to the Government of Panama on the organizational structure and function of the new police, and on general police policy. With monies under the supplemental, it plans to provide up to 10 full-time technical consultants to assist in the implementation of new policies. A model precinct is being established as a testing ground for new organizational principles, police procedures and information systems which would be replicated in other precincts as soon as possible.

In the area of training, ICITAP is focusing on development of a training cadre within the police and a new police academy. It is presenting courses in basic police skills, such as patrol and traffic supervisory techniques and limited use of force, and will assist in teaching the first 20-week basic recruit course at the academy. It is also presenting courses for managers and supervisors as well as leadership seminars for ranking officers focusing on the mission and management of civilian police institutions.

A series of separate development activities are being planned for the technical judicial police, the basic investigative corps assigned to the Attorney General. The immediate need is to reequip the forensic lab and train technician in its use. Training in basic investigative techniques and case management will also be provided for the investigators and prosecutors who work with them.

An overall funding level has not yet been determined. ICITAP estimates that its training and technical assistance activities could absorb $5 million a year and has recommended urgent equipment purchases as well (primarily vehicles and forensic laboratory equipment). The bill limits equipment purchases for the police to $5 million. We presently estimate the projected cost of ICITAP activities under the supplemental at $12-$15 million.

THURSDAY, MARCH 22, 1990.

PROBLEMS IN OUR OWN BACKYARD: WESTERN HEMISPHERE ISSUES

WITNESSES

BERNARD ARONSON, ASSISTANT SECRETARY, BUREAU FOR INTER-AMERICAN AFFAIRS, DEPARTMENT OF STATE

MELVYN LEVITSKY, ASSISTANT SECRETARY, BUREAU OF INTERNATIONAL NARCOTICS MATTERS, DEPARTMENT OF STATE

FRED W. SCHIECK, ACTING ASSISTANT ADMINISTRATOR, BUREAU FOR LATIN AMERICA AND THE CARIBBEAN, AGENCY FOR INTERNATIONAL DEVELOPMENT

HENRY S. ROWAN, ASSISTANT SECRETARY, INTERNATIONAL SECURITY AFFAIRS, DEPARTMENT OF DEFENSE

CHAIRMAN'S OPENING STATEMENT

Mr. OBEY. Good morning. Today we will review the Administration's budget request for the coming fiscal year as it relates to western hemisphere problems. We have as our witnesses: Bernard Aronson, Assistant Secretary for Inter-American Affairs; Melvyn Levitsky, Assistant Secretary, Bureau of International Narcotics; Mr. Fred Schieck, Acting Assistant Administrator, Bureau for Latin America and the Caribbean; and Mr. Henry Rowan, Assistant Secretary for International Security Affairs. Gentlemen, I am going to ask you to each summarize your statement in about five minutes. We have many questions we need to get through by 12:00 o'clock. So keep the bafflegab down if you will.

I would simply ask you to summarize your statements very briefly and then we will get right to the questions. Let me simply say, to put our comments in context Mr. Secretary, we are about to face a vote on the supplemental appropriation. I do not know how tangled that bill is going to become with various issues besides the ones the Administration is focusing on, namely Panama and Nicaragua. I am sure there will be some.

I frankly would prefer to deal with issues such as Salvador for the regular appropriations bill. I do not know whether or not events will allow us to do that. I frankly think we do not do anybody any good by having a range war between the executive and legislative branches on an issue this sensitive.

U.S. POLICY TOWARD EL SALVADOR

I have to say, however, I am extremely frustrated. I think a number of my colleagues are frustrated, also. I personally am convinced there is such deeply ingrained resistance in the Salvadoran military culture to what is ostensibly U.S. policy that in fact we have not, up to now, been able to retain many of the gains that people thought had been made a year ago. I will not go into details. You know what they are as well as I do.

I am going to renew a request which I made to Secretary Baker. I think if we are to deal with Salvador rationally, we need to try to put together the same kind of cross-ideology approach that was, in the end, put together last year on Nicaragua.

I think there is only one way to do that. It does not involve having another debate between your guys and our guys on Salvador. It involves, in my view, having the Administration do what Lyndon Johnson did with respect to Vietnam. Lyndon Johnson asked Clark Clifford to engage in a fundamental review of Administration policy. Mr. Clifford came back and addressed some very serious shortcomings in Johnson's policy, and that policy changed.

I am making no prejudgments about whether your policy should change or not. I do think that if you are to establish a broad-based consensus which can be sustained throughout a period of long negotiations, if in fact we get into negotiations in Salvador, we have to have some action that brings that about.

I think the action that could help do that would be to have the White House announce that it is appointing either an individual or a team of individuals to independently review the policies—our policies now with respect to Salvador—focusing on questions such as the following: Why is it that after ten or twelve years of aid the rebels still can do what they did in their offensive just a few months ago? Why is it the military is not more effective in Salvador? How much chance do we really have to break through the pathology which exists in the Salvadoran military with respect to negotiation and the quaint idea that they should not wipe out people who disagree with them? What standards should we judge the rebels by? What are the specific steps which they and the government need to take in order for both of them to live up to what we are asking?

Questions such as that. There are others, but I do not want to take the time now to get into it.

In my view, if the Administration wants to avoid a continued series of very acrimonious debates on this issue, they should take that action. Short of that, I frankly do not think that we are making sufficient progress in Salvador and I personally do not feel I can vote for Salvador money.

I want to be able to avoid that by having a new consensus built around a clear understanding of the policy changes needed in order to accomplish goals I think we both share. I am asking the Administration to consider that, because I think nothing short of that will prevent the kind of arguments you otherwise will inevitably face on the supplemental authorization, on the supplemental appropriation, on the regular appropriation bill, on the continuing resolution, ad nauseam.

I think it is in your interest and the country's interest to engage in that kind of a fundamental review. I am confident if you do review that policy, you will discover there are some things that need changing. There are also probably some things you can bring us around to support.

Without that kind of approach, I think we are going to be in a year-long range war on an issue we ought to be united upon.

Having said that, let me simply ask you to proceed.

MR. ARONSON'S OPENING STATEMENT

Mr. ARONSON. Okay. Mr. Chairman, I would like to respond to your opening remarks and then perhaps give my brief summary. I do not know which order would be most productive.

Mr. OBEY. Whichever you prefer.

Mr. ARONSON. I do not want to fail to respond, because I think you said some very thoughtful things. Let me just begin on Salvador and then make some opening remarks, and I guess we will get back to Salvador.

I think all the questions that you raised are the right questions and I appreciate the fact that you raised them and in the spirit that you did. And I also fundamentally agree with you that we need to come together with the Congress and look at this question without polemics or rhetoric and try to decide what has worked and what has not and where we have to go.

We did that, as you know, as I said the other day when I came up here to testify on the supplemental, on Nicaragua, which was an equally contentious issue, in some ways more so; it divided us up as nothing like Vietnam. But a year ago we came together and decided we are not going to continue to cut each other up, liberal, conservative, Democrat, Republican; we are going to try to come together and listen to each other and figure out what is the best thing to do for our country.

Because we hammered together that bipartisan accord and did not spend a year fighting over Contra aid, we were able to support these elections and focus attention on them, mobilize a policy and have credibility in Central America for the first time in ten years. And the results are as clear as one needs to see.

EL SALVADOR NEGOTIATIONS

We need to do the same thing in Salvador. I think I have one slightly different perspective. I understand the sense of exhaustion and frustration, and I know that many good people like yourself have tried to stand for a principled policy on Salvador which defends human rights and advances democracy, but has no illusions about the nature of the FMLN.

I also know that the groups that come up here do not say, it is good that we defended the democratic center. There are groups that just have one perspective and all you do is get your brains beaten in. So I think it takes a certain political and moral courage to do that, and I respect you for it.

The only point I would add to that is, one, we are prepared to have that kind of dialogue with you. Whether we will do it by appointing a presidential commission or not, I am not sure. But Secretary Baker is coming back this weekend and I think he and I would like to come up to the Hill to talk about Salvador with you and the leadership and others.

The only optimistic note I would like to leave this initial opening discussion on is that I honestly believe that conditions have never been better in the history of this conflict to end it than they are right now. And in fact, if you had a chance to read the New York

Times today, the two sides are literally on the verge of coming together behind a new set of negotiations which the UN has helped to knit together and of which we have been supportive also behind the scenes, very directly.

The reason that this process has taken longer than some might have hoped is that I think the government of El Salvador, the UN, the United States government, and I hope the FMLN also, have concluded that what we do not need is another round of public relations exercises, of a publicized meeting one day in some city and everybody having their press conferences before they have sat down. Then somebody blows up the negotiations literally or figuratively, and unfortunately it is usually literally.

There has been a lot of hard, patient, behind the scenes work establishing the ground rules for this next set of negotiations, so that they will be ongoing, continuous, and at a senior level.

Already there have been some confidence-building measures taken. As you know, the five Central America Presidents in December in San Jose called on the FMLN to stop attacks on civilians. They have announced a partial agreement to the call of the five Central America Presidents, not a total one, but it was a positive step, and the government of El Salvador said as much.

I believe that the Secretary General will probably be prepared to make an announcement on new talks relatively soon. And the reason I emphasize this point is, as you said, this is a very delicate and sensitive moment, and whatever else we do, let us not rush out of a sense of exhaustion or political imperative to do something that is going to screw this up, because I think we can end this war this year.

As I have said before in open testimony, one of the reasons I took this job was to do that, to help do that, and I think we can. I also believe that if this issue becomes politicized again and we turn it into a partisan fight, that we will once again screw it up. I do not think we can afford to do that and I think the Salvadoran people would rightly condemn us if we did.

Having said that, let me just say something about the hemisphere, because one of the frustrations of my job is that I come to a lot of hearings and people say: How come you are obsessed with Central America? And I never get to talk about the rest of the hemisphere.

Mr. OBEY. Could I just interrupt to say—I will not take your response out of the five minutes, because I appreciate the response. I am going to ask you if you could each limit your opening comments to five minutes, because we have many questions.

Mr. ARONSON. Okay.

Mr. LEWIS. Mr. Chairman, I wonder if I could comment very briefly.

Mr. OBEY. Sure.

Mr. LEWIS. David, I think that that which Bernie has said is an important note for all of us. I know you are frustrated, I am frustrated, with the business of sometimes partisan gibberish getting in the way of real people problem-solving.

I think this committee is way beyond that point and anxious to see is contribute to solutions. So your comments are very welcome and I think, in terms of Central America, right on target, and it is time that we looked at the rest of the continent as well.

LATIN AMERICA ISSUES

Mr. ARONSON. Mr. Chairman, if you go back a year ago and revisit the conventional wisdom about Latin America, it went something like this: that the hemisphere was in crisis; democracy was going to go up in flames and social turmoil. People were writing learned op-ed pages about whether Salinas would survive in Mexico and whether there would be a radical populist alternative.

There were food riots in Venezuela. There was concern about the survival of democracy there. The conventional wisdom suggested that the drug cartels in places like Colombia had won the battle, they were invincible, and the only question was when would the state sue for peace.

General Noriega was believed to have successfully defied the U.S., made us a fool in the hemisphere, was beating the nationalist drum, and would probably either win or steal the election.

The conventional wisdom about Nicaragua was that the Contra policy was exhausted and that the only option for the U.S. was to accommodate to a permanent Sandinista dictatorship.

This is a bit of an advertisement, if you can tell.

In El Salvador, the conventional wisdom was that the prospects for peace were evaporating and that the politics of the country would repolarize and we would have an endless war. And the conventional wisdom about Haiti was that that poor country was condemned to endless instability and dictatorship and repression.

I think none of those things have come about, in large part because I think you have a new generation of leaders in this hemisphere who have watched the ~~way the~~ world has changed and, with a lot of courage, have tried to change their own countries. They have fundamentally concluded that democracy is the only legitimate and stable and defensible form of government and have brought democracy back to their countries, often at great price.

Today South America is entirely led by elected leaders, for the first time in decades. Central America is now led by, or will be on April 25th, by elected leadership for the first time probably in its history.

This Administration, with the support of this committee and the Congress, also tried to be a part of the changes that have gone on for the better. Within five weeks of taking office, we successfully negotiated a major replenishment of the IDB and some new lending policies. We announced the Brady Plan on debt. Mexico was the first successful debt negotiation, Costa Rica was the second. Venezuela has just concluded negotiations. The Philippines also, but they are not in my jurisdiction.

The President and the leaders of the three principal cocaine-producing countries have come together on a joint strategy which is real and has made a difference and will make a difference. The bipartisan accord on Central America permitted us to defend elections in Nicaragua successfully and the outcome I think has opened up real hope for that whole region to both democratize and demilitarize and ultimately develop. We are trying to support the strengthening of the CBI, which is vital for the Caribbean.

But the question that the leaders of this hemisphere are asking really is, can the United States take yes for an answer? They are moving in all the directions that U.S. leaders have urged upon them for decades. Democracy is their watchword. They are opening up their markets, they are privatizing. They are removing barriers to foreign investment. They are realigning exchange rates in terms of market forces.

Their fear is that just at the moment when they are starting to move in directions and according to policies that the U.S. has advocated, that we are going to once again go into eclipse and forget about this region and be diverted by events in other countries.

I hope that the United States does not make that tragic mistake, because one of the lessons we need to understand is that the growth and development of this hemisphere is not just good in some abstract sense for the United States, but it is good for us in terms of our own economic development. Growth in this hemisphere means jobs in the U.S.

Mexico, for instance, is our third largest trading partner today. The last two years, our exports to Mexico have grown 40 percent. And every time we successfully support democracy and market economy and economic development in a country in the region, we mean jobs for farmers and ranchers in Wisconsin, in California, manufacturers in southern Illinois.

ADMINISTRATION'S BUDGET REQUEST

The statement that I submitted for the record goes through our specific request for fiscal year 1991. I will just give you the highlights so I can keep to the five-minute rule. We are requesting $1.4 billion for economic and anti-narcotics assistance in fiscal year 1991 and $296.3 million for direct military aid.

This represents an increase of $261.9 million, or 18.3 percent over levels requested for fiscal year 1990. That primarily is driven by the President's Andean drug strategy and is to strengthen our capacity to take on the cartels.

We have asked for $651.9 million in ESF and $296.3 million for military aid, FMF and IMET, which again reflects our priorities of about three to one economic over military support. That represents in terms of FMS 8.9 percent of the requested worldwide security assistance.

I could go through each country and each request, but I do not think we have time to and maybe we will do that in the questioning. I would like to make one pitch for the supplemental again, even though I was up here for that bill before. We have an opportunity in Panama and Nicaragua to permanently transform the history and landscapes of those countries and this region. But they cannot afford for us to cut the baby in half.

It would be better to do nothing than to raise expectations in those two countries that the United States is going to do something serious and not meet them.

What we have asked for for Panama and Nicaragua may sound like a lot of money, but in terms of the need they are actually very modest requests, and they will make a fundamental difference. Panama, as Vice President Ford has said up here last week, is not asking for a permanent relation of dependency on the United States. They need to jump-start an already resilient economy, and with this supplemental they can do so.

Nicaragua needs to crawl out of a hole that has put them back 50 years, to sustain and consolidate this new democracy, and $300 million is a bare minimum to make that possible. And I hope that the committee will resist extraneous amendments or extra demands that will only water down the package.

[The prepared statement of Mr. Aronson follows:]

Prepared Statement of
Bernard W. Aronson
Assistant Secretary of State
Bureau For Inter-American Affairs
Before The
Subcommittee on Foreign Operations
House Committee on Appropriations
House of Representatives
March 22, 1990

Mr. Chairman, I appreciate the opportunity to discuss with you the Administration's foreign policy priorities in the Inter-American region and our FY 91 foreign assistance request.

The past year has reaffirmed and strengthened the unparalleled transition to democracy in the western hemisphere that has marked the past decade. As in Eastern Europe, this breakout of democracy has dramatically altered the political landscape to our south. Panama, Nicaragua, Chile -- these nations add some 20 million people to the democratic community of the Americas. Haiti too, now has another chance. Our neighbors in the Americas, given a choice, have opted for free government and free enterprise. The dream of the Americas as the world's first fully democratic hemisphere suddenly appears within reach. The challenge to the hemisphere in this, the last decade of the 20th century, is to complete the transformation.

Our policy and our resources played an important role in support of this remarkable trend toward democracy. We have sought to back this trend in each nation of the hemisphere, not only because it reflects our deepest values, but because it is in our interest. We enjoy the strongest relationships with those countries whose governments are founded on the consent of the governed, the only sure basis for respect for human rights, equitable development and the dignity of the individual.

We have an opportunity and a responsibility to continue to support the expansion, consolidation and development of democratic gains in Latin America and the Caribbean. Our policies have put us on the right course. We must keep moving on that course. And we must have the resources to get the job done. Were we to become complacent now, we could lose some very considerable gains; we would surely miss some crucial opportunities.

A bipartisan approach offers us the best chance of achieving our key objectives. I look forward to working with you and the subcommittee, Mr. Chairman, as we chart our policy priorities ahead.

The ability of this team effort to deal with the challenges of the '90's, particularly those that threaten the economic well-being of our region, faces a tough test in the coming year. High inflation, underdevelopment, and debt continue to restrict growth and undermine the stability of still fragile democratic governments. Our will to continue what we have begun is also being questioned by the region which sees Latin American economic and financial needs being marginalized in a rush to develop Eastern Europe.

Our contribution to economic development and to security, without which there would be no development, in Latin America and the Caribbean has been substantial in the past. To protect our investment, we will need to maintain a sustained level of support in both of these areas. And we must do so despite the competition for resources among the many crucial national interests at stake in other regions of the world. A stable, democratic and prosperous Latin American and the Caribbean can become even more profitable markets for U.S. goods and services, partners in productive commerce and investment. A region which creates sufficient jobs for its growing population also restrains illegal immigration.

Before we discuss the specifics of our FY 91 assistance request, I would like to set out four regional tasks facing us in the '90's, toward which we need to direct our energies and resources.

The four tasks are: consolidating and building on democratic gains, advancing economic development, promoting peace, and ridding our region of the scourge of drugs.

Consolidating Democracy

The first task, consolidating and building on democratic gains, is our top priority. In the cases of Nicaragua, Panama, Chile, and other countries of the region, a new generation of democratic leaders is emerging. The people of these countries have stated what they want: an open society, basic human rights and civil liberties, democratic political institutions and the chance to build a stable and prosperous future for themselves and their families. The challenge for the new leadership is to respond to the heightened expectations of improved political and economic conditions.

In Nicaragua and Panama, the tasks of political and economic reconstruction are massive. We must seize the opportunity to demilitarize the region, build the peace and democratic institutions. These new democracies will need court systems that are fair, free and reliable police forces that are free from corruption, free trade unions and other democratic institutions. All this will require our and international support, including that of other western democracies. The UN and OAS also have roles to play in helping to enforce and verify compliance with the Central American peace process.

Meanwhile, Colombia, engaged in a mortal struggle with the drug cartels, prepares for a presidential election this Spring. Further south, Chile has peacefully ended 17 years of authoritarian rule and political isolation. Argentina, Brazil and Uruguay have successfully transferred power from one democratic government to another. Paraguay has entered the democratic ranks. In the Caribbean, Grenada held free elections this month, further consolidating its transition to democracy. In Haiti, President Trouillot, who has provisionally replaced General Prosper Avril, backs free elections and has promised to pass power to a democratically elected government. In our view, fair and free elections under international supervision offer the best hope for ending Haiti's longstanding suffering. Elections are also scheduled in May for the Dominican Republic -- the most populous nation in the democratic Caribbean where politics, allowed to flourish in the past quarter century, have become as popular as baseball.

Advancing Economic Development

Advancing economic development, our second task, remains a major challenge. Strengthening of democracy and democratic institutions will depend importantly on a rising level of income and prosperity. However, during the 1980's, the predominant economic trend for the region as a whole was one of low growth, falling per capita income and rampant inflation.

From 1981 through 1989, real per capita gross domestic product (GDP) declined in the region by over 8 percent. This is in stark contrast to the region's strong economic growth between 1960 and 1980, during which real per capita GDP rose by more than 80 percent. Overall GDP in the region grew during the last decade by less than 12 percent. This masks the fact that in some countries, overall GDP actually fell for a number of years. Meanwhile, inflation, which soared to a startling 1,000 percent on a regionwide basis in 1989 continues to undermine the social fabric and political stability throughout the region.

Argentina, Peru and Brazil are now grappling with hyperinflation and continue to face an array of economic problems which vividly illustrate the principal underlying cause for the region's poor growth during the decade -- inappropriate economic policies.

Many of the region's countries, including Argentina, have begun to reorient and restructure economic policy. Brazil's new President has announced a program of comprehensive economic reforms. Impressive progress has been made or begun by such diverse countries as Chile, Mexico, Costa Rica, Colombia, Guyana, Bolivia, Uruguay, Jamaica, Venezuela, El Salvador, and Paraguay.

There seems to be a general recognition throughout Latin America -- indeed, throughout the world -- that development can advance only by discarding ingrained statist, inward-looking policies, and moving toward private-sector driven, trade-oriented economies. But change does not often occur quickly. And profound structural economic adjustments involve wrenching societal costs. On a regional basis, investor confidence is still low because the reform process has been slow and uneven. Availability of capital will remain a critical problem in the 1990's.

Foreign indebtedness also remains a major stumbling block to growth. Progress has been made, especially this past year under the Brady Plan in reducing the region's external debt. Most recently, Venezuela has reached a debt reduction agreement with the banks. But for many countries, especially those with heavy official debt burdens, such as Jamaica, and those undertaking difficult reforms, the burden of servicing external debt will continue to hinder economic growth.

Latin America and the Caribbean face a twin development challenge in the 1990's. First, democratic governments must meet the demands of domestic constituencies for economic stability and prosperity. Second, the region's countries must take action to ensure that they are isolated no longer from the economic opportunities presented by a rapidly changing and increasingly interdependent world. The quickness of newly-emerging democracies in Eastern Europe to capture the world's attention and to make fundamental economic changes makes Latin American reforms all the more urgent as a basis for competition.

The first step -- and the most important one -- must be taken by the region itself. Open markets relying on private enterprise are key to broad-based and sustainable growth. Latin American and Caribbean governments must keep moving ahead to complete the reform process. But we can -- and must -- help.

For the peoples of Central America and the Caribbean, the Caribbean Basin Initiative (CBI) is a symbol of U.S. commitment to open markets and free institutions. Its investment and trade benefits drive much of the Basin's economic vitality, and contribute to a more prosperous, democratic, and stable region.

More than ever, CBI and the free market principles it represents must be the engine of growth. CBI has achieved rather dramatic successes, broadening and diversifying the region's exports.

In November 1989, the President called for enhancement legislation to consolidate and build on gains under the original bill. Last year, the House passed an enhancement bill repealing CBI's 1995 expiration date, crucial to maintaining investor confidence in the region. The Senate Finance Committee marked up its bill earlier this month, and I am gratified permanent extension is part of that bill as well.

I continue to hope, however, that Congress will not only extend CBI, but will strengthen it, particularly in areas currently excluded from duty-free treatment especially textiles and non-leather footwear. I know that these are sensitive issues domestically; however, I am convinced we can craft provisions which do not threaten U.S. industry, while offering meaningful new benefits to the Caribbean Basin.

Our Economic Support Funds (ESF), and the policy dialogue which accompanies them, are critical for a number of countries in the region, to support economic stabilization and structural adjustment and economic reform programs that take several years to implement. Our ESF for Jamaica is a case in point; Prime Minister Manley is moving forward with a sustained adjustment effort that would be seriously undercut without our help in 1990-91. We need ESF for Guyana where President Hoyte has undertaken similar reforms and an international support group which has our strong backing has received a pledge for U.S. assistance which we have been unable to supply for lack of resources. ESF in the Dominican Republic will encourage a new government to enact needed economic measures.

ESF for Bolivia and Peru will be designed to help them face the major challenge of restructuring their economies away from reliance on revenue from narcotics. In the case of Colombia, ESF will help relieve the economic burden of its courageous war on the cartels.

Costa Rica and Guatemala have established a solid record of economic growth over the past several years as the benefits of economic reforms which both countries undertook several years ago have been felt. Economic growth in El Salvador and Honduras, while positive, is small. Both countries have recently adopted wide-ranging fiscal, monetary, trade and other economic reforms aimed at lifting growth rates.

El Salvador has been battered this past year by the fall in coffee prices on top of the economic cost of the continuing military conflict. Yet, President Cristiani remains absolutely committed to a modern, efficient, market-oriented economy. So serious is his administration in making these reforms that the Salvadoran assembly ratified a major set of tax, tariff and trade measures on November 30 of last year, while the offensive was still underway.

The Honduran government is just as serious about its economic reform program. On March 2, 1990, President Callejas presented a sweeping, historic economic restructuring package to the nation. The very next day, the Honduran Congress approved the measures.

We believe that our ESF levels to the Central American countries must be kept commensurate with the seriousness and short-term costs of these essential reforms. Costa Rica, Guatemala, Honduras, El Salvador are all now moving in the same economic direction - towards free-market and efficient economies. Mrs. Chamorro will launch Nicaragua on the same path beginning on April 25th. These economic reforms, supported by our ESF, lay the groundwork for the ultimate objective: self-sustaining, equitably spread economic growth in all countries of the region. We must stay the course to finish the work defined by the 1984 National Bipartisan Commission on Central America. Political stability and the opportunity to end regional conflict is far closer today than a year ago; we need to hold steady until this promise can pay off in a new era of peace, stability and development for all the people of that troubled region.

Lack of flexibility and reduced ESF levels for the region prevented allocation of significant FY90 ESF for the Caribbean region. ESF has a major impact on such small economies. The wide year-to-year fluctuations in funding make it very hard for these governments to plan fiscal and other policies. ESF also serves to recognize the Caribbean commitment to fighting drug trafficking even with limited managerial and physical resources. As traffic gets diverted from established sea and land routes, the Eastern Caribbean offers an almost irresistable "target of opportunity" for traffickers. Our small neighbors cannot meet this challenge alone.

Economic development is entwined with the political process. As noted earlier, a civilian interim president in Haiti has promised free elections as her top priority. Our FY91 request includes ESF for Haiti to be used to reinforce democratic processes and meet urgent economic needs. It would only be obligated, however, after consultations with the Congress, and the clear agreement that our common democratic goals are being met. Elsewhere democracies are already established and ESF programs for the press, labor unions, and legal institutions contribute to deepening the democratic process, promoting democratic values, and, at the same time, making the rules of economic activity more transparent and equitable.

Promoting Peace

Our third task is promoting peace. President-elect Chamorro's overwhelming victory in the February 25 elections in Nicaragua and President Ortega's conciliatory public statements bode well for a successful transition on April 25 to a more democratic, Western-oriented regime with a modified free market economy. Nevertheless, we are disturbed by reports that:

-- The outgoing Sandinista regime is distributing weapons to loyal followers;

-- That supplies of petroleum and basic foodstuffs are being run down, in an effort to exacerbate shortages and create unrest after the inauguration; and

-- That the Sandinistas are sacking government offices of supplies and equipment, and distributing other government property as rewards to loyalists.

We have urged the Nicaraguan Resistance to demobilize and reintegrate into Nicaraguan civilian society. But, we can only do so responsibly if mechanisms are in place to assure their safety and give them economic alternatives. The Sandinista Government has insisted frequently that the Resistance demobilize immediately, but it has refused Cardinal Obando y Bravo's request to bring Resistance negotiators to Managua to meet with him and the incoming and outgoing governments to work out practical arrangements for demobilization. The time for posturing on this issue is over. The time has come for all parties to cooperate on solving this human problem and promoting the national reconciliation that Violeta Chamorro has called for.

In the period leading up to April 25 and beyond, the U.S., working with international organizations such as ONUCA and CIAV, must address the legitimate security concerns of the Nicaraguan Resistance, as well as support repatriation and assistance programs that will allow the resistance to resume a role in Nicaraguan society.

In order to facilitate that task of national reconstruction and reconciliation, on March 13 President Bush asked Congress for $300 million in immediate economic aid to the Chamorro government to help rebuild Nicaragua's prostrate economy, particularly its agricultural sector, and announced an end to trade sanctions imposed five years ago against the Sandinista regime.

In El Salvador, we are encouraged by the FMLN's announcement on March 13 that it is willing to end attacks on civilian targets in order that peace talks with the Cristiani government -- broken off by the guerrillas last year in conjunction with their devastating assault on San Salvador in November -- may be resumed soon under the good offices of UN Secretary General Perez de Cuellar. The UN has been seeking for several weeks to facilitate talks between the Salvadoran government and guerrillas. The FMLN publicly announced on March 13 that it would unilaterally suspend some attacks against civilian targets, but reserved the right to attack the electrical power grid and to kill civilians "engaged in military and paramilitary activities." The Salvadoran government immediately acknowledged the positive elements in the FMLN announcement. The Salvadorans complained, however, that the FMLN announcement was a breach of confidentiality that both sides had agreed upon in requesting UN facilitation. We fully support the UN's efforts to get the two sides together, and believe that the government's positive response to the FMLN suspension of some hostilities will move the process forward.

We are also encouraged by the recent successful repatriation of thousands of Salvadoran refugees living in Honduras and hope that this will set a precedent for similar efforts on behalf of Nicaraguan refugees living in Honduras and Costa Rica.

Attacking Drugs

The traffic in illegal drugs has emerged as a threat to democracy and stability in this hemisphere. As Secretary Baker told the Senate Foreign Relations Committee last month, ultimately, the illegal narcotics trade robs not only individual users but entire nations of their freedom. Further, he said, "The drug pirates and profiteers attack the central nervous system and vital organs of government: the administration of justice, the integrity of government, the right of free speech. That is what happened in Noriega's Panama."

Our Administration has advanced a determined strategy to confront the cocaine crisis in our hemisphere. It is a comprehensive strategy which balances demand reduction, enforcement and military action with U.S. economic assistance in the Andean region, in particular Colombia, Peru and Bolivia. The strategy is made possible by the deepening understanding between us and the Andean countries with whom we face a common threat. It is a promising start but it will not succeed if we do not follow through on our efforts to broaden our assistance to these countries in their struggle against the drug scourge. Certainly, we will encourage the international community to contribute generously as well. But we must acknowledge and assume our responsibility to lead the way.

In signing the Declaration of Cartagena on February 15, President Barco and his Andean counterparts endorsed a multinational approach to the drug problem. They committed their governments to stepped-up efforts in the war against the illicit drug trade, both bilaterally and through regional cooperation in the OAS. Our budget request seeks military and economic assistance, trade cooperation and alternative development aid to help fight the drug war. The latter is particularly important to strengthen the legitimate economies of the Andean nations and provide alternative economic opportunities to the farmers now growing coca leaf.

Elsewhere in the region, the Caribbean and Central America are natural drug transitting routes, caught between South America producers and North American consumers. The small countries of the region do not have the resources to take on the well financed drug cartels. Moreover, the spill over effects of trafficking is creating domestic drug problems on an ever growing scale. Drug traffickers continue to use their evil gains to corrupt police officials who, given low salaries, often fall prey to offers of big money.

Overview of our Budget Request

I would like now to discuss the Administration's request for assistance for Latin America and the Caribbean for FY 91. These requests balance vital interests of the United States with the need to meet head-on the four tasks I have outlined earlier.

For FY 1991, we are requesting $1.4 billion for economic and anti-narcotics assistance and $296.3 million for military aid. This represents an increase of $261.9 million, or 18.3 percent over levels requested for FY 1990. In real terms, the increase is about 17.6 percent. The total requested, $1.696 billion, accounts for a little over 14 percent of our worldwide assistance request.

Security Assistance

I will now discuss the security assistance component of our request.

For FY 1991, we have asked for $651.9 million in ESF and only $296.3 million for military aid (FMF and IMET), totaling $948.2 million, or 8.9% of requested worldwide Security Assistance.

Of the military aid requested, $13.19 million will go to the International Military Education and Training (IMET) program. This will provide first class professional and technical training to Latin American officers and NCOs. It will also expose the future military leaders of the hemisphere to our values with respect to human rights -- as well as to our model for the role of the military in a democracy. It is a fact of life that, in many countries, the military is an important institution whose leaders often move on to assume positions of political importance. At a very low cost, IMET affords us access to leaders and future leaders. This is particularly important in the emerging democracies of the Southern Cone where the use of IMET has been interrupted over the past years to the point that that there is almost a generation of officers who have not been exposed to U.S. training. For these reasons, we are requesting IMET programs in virtually every country in Latin America and the Caribbean with which we maintain diplomatic relations.

Of the $283.1 million Foreign Military Financing (FMF) we have requested, $139.0 million will support the President's Andean Counternarcotics strategy in Bolivia, Colombia, and Peru. (It also includes $2.0 million for Ecuador. A total of $135.5 million FMF will support key democratic countries in

Central America. Thus, we are requesting only $8.6 million in FMF aid outside the Andes and Central America. Of that amount, $7.1 million is for the drug-plagued Caribbean. The remaining $1.5 million will support improved civil-military relations in the key re-emerging democracies of Argentina and Chile.

Conclusion

Addressing the difficult tasks of the '90's is a challenge. Given the prospect of fiscal austerity and tight international affairs funding over the next several years, it will be imperative to make every dollar count. We will do that, Mr. Chairman. At the same time, we must all guard against the appeal of false economies, particularly where smaller programs are concerned, lest we risk missing substantial opportunities to promote U.S. interests for the sake of savings that mean very little for our overall budget picture. We have a unique opportunity to take advantage of positive world and regional trends to secure peace and stability in Central America. We must provide the resources necessary to assure that the people of this troubled region can escape from a decade of civil conflict to consolidate their democracies and rededicate themselves to development.

You can help us in one very key way: reverse the trend toward earmarks. Throughout Latin America and the Caribbean, U.S. assistance in advancing economic development requires careful planning and the ability to respond flexibly to take advantage of new opportunities or to meet crisis situations. As we have seen in the current fiscal year, extensive earmarking has served only to reduce the flexibility and effectiveness of our assistance programs. Let me join the Secretary of State, Mr. Chairman, in proposing that we make legislative earmarks a last resort, to be avoided if at all possible. Instead, let us work together to explore ways to achieve greater flexibility to respond to the dynamics of change in our region.

The movement towards a new era of democracy, open economies, and peace in our troubled region makes this an especially exciting time to be working with Latin America and the Caribbean. We can justly be proud of our contribution in helping events unfold positively. It is an investment well worth protecting. As we look to the future, I know that we can count on your committee, Mr. Chairman, to work with us in nurturing the delicate forces of democracy, prosperity and stability in our hemisphere.

Mr. ARONSON. Mr. Chairman, I do not guess we introduced the other members of the panel, or did you?

Mr. OBEY. Yes.

Mr. ARONSON. Okay. Well then, you might want to call on them or we will take questions, whatever you want to do.

Mr. OBEY. All right. Mr. Levitsky, did you want to add anything?

MR. LEVITSKY'S OPENING STATEMENT

Mr. LEVITSKY. Well, I will try to make, I hope, the Guinness Book of World Records short statement.

You have my longer statement, which goes into the totality of our drug strategy, including not only the western hemisphere but throughout the world. I would, since we are focusing on the western hemisphere, let me just say we have a comprehensive strategy contained in the two documents the President has issued in September and February. That deals comprehensively with our narcotics control efforts.

We have an Andean strategy and we have a cocaine strategy that we have submitted to the Congress, which contains all the elements. So I will not go into that.

I would say in general there are a lot of problems, as there are in every country with regard to drugs, corruption, ineffectiveness, inefficiency, lack of political will. We have made a good deal of progress this year in building institutions. Cartagena has been the centerpiece in this hemisphere.

My Bureau is asking for $150 million in 1991. $87 million of that we would plan to spend in Latin America for three purposes: to strengthen the political will and institutional capability of the three Andean governments; to increase the effectiveness of the military and law enforcement activities against the coca trade; and to inflict significant damage on trafficking organizations.

The heart of the strategy is in the Andean region, but the strategy also applies to surrounding countries and transit areas through which cocaine flows. Mexico is a key here. It has improved its efforts during the year and we are asking for an increase for the Mexico program as well.

So that we look forward to further success in 1990 and 1991, and with these additional resources we are confident that we can accomplish that.

Thank you.

[The prepared statement of Mr. Levitsky follows:]

STATEMENT
House Appropriations Committee
Subcommittee on Foreign Operations
Assistant Secretary of State
for International Narcotics Matters
Melvyn Levitsky
March 22, 1990

Mr. Chairman:

I am pleased to appear here before you today to summarize the Department of State's FY 1991 budget request of $150 million for the Bureau of International Narcotics Matters. Our budget, which we have submitted formally to the Committee, contains program details and justifications.

Our request is approximately $36.9 million, or 31 percent, over the FY 1990 appropriated level and builds upon enhanced counternarcotics efforts in the Andes in FY 1990. Before discussing the details of our request and providing the Committee with further justification, I would like to share some thoughts on what we accomplished over the past year, and where I see INM going during the next year.

Mr. Chairman, a number of critical narcotics control developments took place during 1989, in priority regions of South America, Mexico and the Caribbean. Cocaine seizures increased over previous years; Colombia seized 37 metric tons of cocaine, and Mexico seized another 34. Colombia's crackdown against drug traffickers has disrupted part of the cocaine trade, and drug dealers are no longer able to live the high life they had taken for granted. There is more evidence that the pressure is working: coca leaf prices in Bolivia and Peru are dropping, leading peasants to seek legitimate alternatives. During 1989, we were able to complete a secure base in Peru's Upper Huallaga Valley; this base enables Peruvian and U.S. law enforcement personnel to now conduct regular operations against cocaine manufacturing and trafficking.

The historic meeting in Cartagena signalled a new era in narcotics cooperation with our Andean partners. No longer is the drug issue simply a law enforcement problem; we are committed to working with Colombia, Bolivia and Peru to explore ways to strengthen military and economic cooperation, including opportunities for expanded trade and investment. The President's $2.2 billion five-year Andean Strategy seeks to bolster these countries' capabilities to attack the drug trade on all fronts.

We know that our efforts to eliminate cocaine trafficking will face many challenges in the years ahead. Coca production continues to increase. Trafficking patterns continue to flow through the Caribbean and Florida and increasingly flow through Mexico and our Southwest border. Central American countries are increasingly important links in the cocaine chain. Corruption still undermines progress in the Andes, in Mexico, Central America and the Caribbean. Violent retaliation by drug traffickers and insurgents threatens efforts to eliminate cocaine production and trafficking.

And cocaine is not our only problem. We are concerned about the possibility of a heroin epidemic, especially given the increases in opium production in Southeast Asia and Guatemala. We have limited political access in most of the major opium poppy producing countries--Burma, Afghanistan, Iran, and Laos. We are concerned that the heroin trafficking situation in bordering countries is worsening. Our concern, however, is being matched by our resolve to develop workable strategies for improving the situation. The Department of State is currently leading a government-wide effort to develop a realistic plan for enhanced heroin control activities.

I am encouraged by the positive developments of 1989 and challenged by the problems still facing us. During the past nine months since becoming Assistant Secretary, I have attempted to bring balance into our programs, enhance our ability to manage these important programs, and work within the Department to ensure that narcotics is a top priority in foreign policy.

Beyond a doubt, narcotics control has become a key foreign policy issue in our hemispheric relations, and is continually viewed as a framework for discussions both with our European allies and drug producing nations. The narcotics issue has the Secretary's support, evidenced, for example, by his public statements, most recently before the United Nations last month. A Narcotics Issues Coordinating Structure has been established within the State Department to raise critical issues which can impact drug control progress.

One of my first tasks after confirmation was to seek the necessary resources to get the job done. The Department has manifested its increased support for the Bureau's activities by granting an additional 25 full-time permanent direct-hire State Department positions. I have reorganized the management structure of the Bureau. I am pleased to note that we have attracted a much larger number of exceedingly able Foreign Service bidders in this cycle and have filled nearly all of our jobs or identified candidates to begin this summer.

We still face many challenges such as planning, implementing and overseeing a complex interregional aviation support function and designing effective diplomatic strategies to involve the multilateral organizations and the European community in more productive ways to reduce the availability of illicit narcotics. I look forward to these challenges in my second year and will seek your support to help me with this task.

Now to the budget. As I stated in my opening paragraph, the FY 1991 budget contains increases that are designed to accomplish three things:

(1) Continue the momentum begun in FY 1990 in the cocaine source countries in the Andes, and support added emphasis on transit nations and the heroin producing countries;

(2) Increase our influence on the multilateral international organizations, such as the United Nations and the OAS, to become more effective in planning drug control projects in producing countries that support our overall national strategy; and

(3) Increase, through interregional training and institution building in source and transit nations, foreign governments' ability to enforce their laws and reduce the supply of narcotics destined for the United States.

The Andes

Over $25 million of the $36.9 million increase requested in FY 1991 is to continue to improve law enforcement programs in Bolivia, Colombia and Peru.

The Administration recently completed a comprehensive, interagency plan that began in June 1989 on how to work with the three major Andean governments to disrupt and destroy the growing, processing, and transportation of coca and coca products within the source countries, so as to reduce the long term supply of cocaine from these countries to the United States. In late August 1989, the President directed that a five-year $2.2 billion counternarcotics effort begin in FY 1990 by augmenting the law enforcement, military, and economic resources in Colombia, Peru and Bolivia. After much deliberation between the United States and the individual cooperating governments, implementation plans have been prepared, discussed and are being refined into bilateral project agreements. After appropriate notification and consultation with the Congress, the Administration intends to allot the increased security assistance, authorize signature of obligating project agreements and begin implementation of the Andean action plans. Although INM exercises policy control over the entire counternarcotics Andean strategy, the Bureau directs the implementation of only the law enforcement portion, or $54.7 million of the approximate $400 million total.

The Andean counter-narcotics strategy contains three major objectives. First, through concerted action and bilateral assistance, it is our goal to strengthen the political will and institutional capability of the three Andean governments to enable them to confront the coca trade. With elections drawing near, the political environment in the Andean countries may heat up. It will be critical to be ready with actions ranging from expanded public diplomacy in each country to encouragement to enact tougher and more effective drug laws in such areas as extradition, money laundering and asset forfeiture.

Second, another major objective of this strategy is to increase the effectiveness of the military and law enforcement activities against the coca trade in the three source countries, particularly by providing air mobility for both military and police forces. Specific objectives include efforts to isolate key coca growing areas, block the shipment of key precursor chemicals, destroy existing labs and processing centers, control key air corridors, and reduce net production of coca through aerial application of herbicides when it is effective to do so.

Third, the final overall goal of the implementation plan is to inflict significant damage on the trafficking organizations which operate within the three source countries by dismantling operations and elements of greatest value to the trafficking organizations. Through strengthening ties between police and military units and creating major violator task forces to identify key organizations, the bilateral assistance will enable host government forces to target the leaders of the major cocaine trafficking organizations, impede the transfer of drug-generated funds, and seize their assets within the United States and in those foreign nations in which they operate.

A major tenet of this strategy is the incorporation of expanded economic assistance beginning in FY 1991 to support the political, legal and military resolve necessary for effective narcotics control action in FY 1990 and beyond. The assistance reflects our conclusion, incorporated in the Declaration of Cartagena, that a comprehensive, intensified counternarcotics strategy must also include understandings regarding economic cooperation, alternative development and encouragement of trade and investment. Our efforts will be directed toward offsetting the negative economic dislocations that are associated with successful narcotics suppression efforts. Loss of hard currency and income alternatives will force certain dislocations that certainly will strain the resolve of the governments.

As pressure is exerted on cartels in the three principal coca producing countries, they will attempt to shift their operations to other countries in Latin America and the Caribbean. Latin American countries most vulnerable to this "spill-over" effect are Ecuador, Venezuela, Paraguay, Argentina, Chile and Brazil. State, in cooperation with ONDCP, will undertake a review to determine how best to assist these countries with their counternarcotics efforts.

Mexico and Transit Countries

We are also requesting additional resources to support the Mexican Attorney General's eradication and interdiction program and improve our coverage of transit zones throughout the hemisphere. We are encouraged with the substantial progress that President Salinas has made in narcotics control since coming to office last year.

President Salinas has elevated the narcotics threat to a national security issue and has taken aggressive action in his first year in office. The past few years have seen an increase in the amount of cocaine entering the United States across the Mexican border; it is estimated that at least half of the cocaine entering the U.S. is transshipped through Mexico. In 1989, the Salinas Administration seized 34 metric tons of cocaine, exceeding the amount seized during the previous six years.

We are requesting an increase of $3.3 million, or approximately 20 percent, over the FY 1990 level to support the expanded use of the Mexican airfleet. To counteract the increased use of the southwestern border as an entry port for cocaine, Mexico has increasingly used its airfleet to support cocaine interdiction operations, including the transport of police personnel, confiscated drugs, and detained traffickers.

The Government of Mexico (PGR) has dedicated increased resources to its anti-drug operations. For example, the PGR increased its budget to $37 million in 1989 from $23.1 million in 1988. The Salinas Administration reorganized and strengthened its drug forces and established a special anti-narcotics interdiction force of 1,500 personnel. The PGR has also increased significantly the size of its airfleet since 1987, adding 19 new helicopters and a number of confiscated fixed-wing aircraft, raising the fleet total to 110 by the end of 1989. Additionally, Mexican military forces continue to perform important anti-narcotics roles.

In addition to continuing to support law enforcement initiatives (e.g., eradication and interdiction, information sharing, etc.), we will seek to strengthen Mexico's ability to track illegal money and firearms flows and the diversion of essential and precursor chemicals. We plan to examine the possibility of integrating financial investigations, munitions control, and essential precursor chemical diversion programs with related U.S. programs. We will also enhance law enforcement investigative lead-sharing, building on, among other foundations, the recently-ratified U.S.-Mexican Mutual Legal Assistance Treaty which we hope to put into force soon. We will also assist Mexico in identifying clandestine labs, landing strips, cache sites, and smuggling routes. Public awareness and demand reduction programs will be pursued through the media, expert visits, training and assistance with community and school education and drug abuse programs.

Finally, an interagency review of narcotics cooperation with Mexico is under way to develop a comprehensive package of proposals for discussions with the Mexican Government which can lead to a new level of counternarcotics cooperation.

Central America and the Caribbean

The narcotics control problem in Central America and the Caribbean is twofold: first, as interdiction has become more successful in certain areas, Central America has increasingly been used as a transshipment point for cocaine. Marijuana and opium have also been grown in certain countries in the region. Second, favorable financial conditions and banking laws made some countries in the region particularly favorable money laundering centers.

In Panama, the Endara Government has demonstrated its commitment to narcotics control and to cooperating with the U.S. in concrete and signifcant ways, including the signing on January 10, 1990 of a basic counternarcotics agreement with the U.S. (Chiles Amendment requirement). In Belize and Guatemala, we plan to continue our eradication and interdiction support. Diplomatic efforts need to focus on raising public awareness, improving joint information coordination centers to improve enforcement efforts, and promoting anti-drug self-sufficiency, regional cooperation and multilateral involvement in narcotics control.

Our bilateral assistance funded by the Latin America Regional program has averaged $6.0-$7.0 million annually for the past several years and we are proposing to maintain that level for FY 1991. Assistance provided includes training, provision of equipment and technical guidance. In FY 1990, we assigned personnel to new Narcotics Assistance Units in Panama and the Dominican Republic.

ASIAN PROGRAMS

The INM FY 1991 budget reflects the limitations of our diplomatic relationships with Myanmar (Burma), Laos and Afghanistan and looks for multilateral strategies where appropriate. Increased heroin production in the Golden Triangle and Golden Crescent areas of the world requires, however, imaginative enforcement/eradication initiatives. The focus, therefore, is placed on capitalizing upon opportunities to control narcotics production and trafficking in Thailand and Pakistan, with funds budgeted for Laos should our ability to influence and work productively against narcotics materialize in FY 1990 as planned.

The "Golden Triangle" countries of Thailand, Myanmar (Burma) and Laos will produce an annual opium crop estimated in excess of 1,500 metric tons in 1988 and 1989; the bulk of this opium comes from Myanmar and Laos. Operations in Myanmar, however, have been suspended due to the current political situation.

Laotian production of opium, heroin and marijuana continues to present severe problems because cultivation and trafficking are expanding. In late FY 1989, the U.S. Government signed a program agreement with the Laotian Government. This agreement will provide alternative economic incentives for producer regions through the development of alternative crops to reduce and eventually eliminate dependence on opium cultivation in Laos.

Thailand's opium production continues to decline due to its effective crop control policy. The FY 1991 budget provides funding to help the Royal Thai Government further reduce opium poppy cultivation by continuing "bridge" assistance to farmers who agree not to cultivate poppy or whose poppy crop is eradicated. The major shift in Thailand, however, is to support Thai enforcement agencies' efforts to stop the flow of opium transiting the country; this initiative will require an increase in new and replacement enforcement equipment.

Opium production in the Southwest Asian countries of Afghanistan, Pakistan and Iran is estimated at 1,109 to 1,415 metric tons in 1989, with prospects for reductions only in Pakistan where a modest aerial spray program was implemented during the 1987 and 1988 crop seasons. In response to the serious increases in opium cultivation, the Government of

Pakistan has enforced the poppy ban in all settled and merged areas with (or without) the promise of development projects. Pakistan has also accepted restrictive poppy clauses which commit the Government to keeping the U.S. Government's Agency for International Development's (USAID) project areas free of opium poppy.

In FY 1991, the Department will continue to support the extension of Pakistan's ban on opium poppy cultivation to the Bajaur and Mohmand regions by introducing improved agricultural crops and by providing income alternatives through an integrated rural development scheme, including roads, wells and electrification. Due to the rapid progression of these projects, the Department is increasing its support for the time-phased enforcement of the poppy ban in these areas. Moreover, the Department will continue to pursue other outreach activities to prevent the spread of opium poppy cultivation and help poppy growers substitute other new crops in areas where there are no major development assistance projects. The Department will give added support to Pakistan's law enforcement and interdiction efforts against trafficking organizations.

Interregional Aviation Support

In FY 1991, the program will support the overall maintenance, hangaring and operational costs for the 52 Department-owned aircraft used in aerial and manual eradication, interdiction operations, survey and logistical support activities. The principal focus will continue to be in Peru, Bolivia and Colombia, with secondary support to Central America and the Caribbean. The aircraft are maintained by a United States contractor and deployed from an air base in Florida. The full deployment of these aircraft will require the additional maintenance and operational funds requested in this budget.

Multilateral Organizations

Our request for voluntary contributions to the UN goes from $3.0 to $5.0 million in FY 1991 to encourage the multilateral organizations to undertake more effective programs in cooperation with drug source countries. By increasing our contribution to the international organizations we believe that we can have more direct influence within these deliberative bodies and expand anti-narcotics projects.

We are also requesting increases for the interregional training program and our program development and support category to fund the annualization of the personnel increase we received in FY 1990.

Mr. Chairman, I believe that we have opportunities in the coming year for meaningful gains in international narcotics control. I know that progress will not be made overnight, and that we will be successful only if we receive the full support of the international community. Thank you for this opportunity to discuss our budget request with the Committee, and I will be happy to answer any questions you might have.

Mr. OBEY. Thank you.

Mr. Schieck.

MR. SCHIECK'S OPENING STATEMENT

Mr. SCHIECK. Thank you, Mr. Chairman.

I have submitted a written statement for the record. I would like to comment on one real aspect of what we in A.I.D. believe is so important about our economic assistance programs.

We have noted, of course, that there are important changes underway in Latin America and the Caribbean. Democratically elected governments are in office throughout the region, governments that are responsive to the will of the people. Concurrent with these profound political changes is the process of economic liberalization. These new leaders understand that economic growth is critical in helping satisfy the basic human needs of the people. To do this, they are willing to change, and in fact are actively changing, longstanding economic policies which have stifled growth in these countries.

They no longer see the need to protect inefficient industries. They see the need to promote exports, to promote non-traditional agriculture, and to allow entrepreneurial spirit to develop and to flourish in their countries.

In many cases, particularly where we have access to ESF funding, A.I.D. and the U.S. Government have been able to play a key role in encouraging this process of policy reform. This is particularly the case in Central America. In fact, I would say that without the Economic Support Funds, it would not have been possible for Central American governments to make the changes which are now resulting clearly in positive growth patterns and broadly based benefits.

We get somewhat frustrated when people say that all the economic assistance in El Salvador really has not produced anything. We get frustrated because we think people need to look at where Salvador was before we started and where it is today.

It is a country which has faced a major insurgency during this period of time, where clearly there was discouragement of investment, where people were reluctant to put resources into the country. But yet the government has struggled, both the previous government and the new government, to adopt policies which are changing that situation.

The growth there is not as much as we would like, but it has turned positive and that is a lot better than it used to be.

I know, Mr. Chairman, that you and the members of this committee last year worked on the problem of earmarking and trying to limit the practice. I believe that nowhere has that problem been more apparent than in the Caribbean, where, because of the combined impact of earmarking and a reduced level of overall assistance, we went from a request level of ESF of around $60 million to only $5 million. Unfortunately some of the important friends of the United States in that region were completely cut off as a result.

We hope that we can renew this effort this year, because it is important, I think, for the United States to be able to respond to legitimate needs of these countries.

I look forward to answering your questions. Thank you.

[The prepared statement of W. Schieck follows:]

PREPARED STATEMENT OF
FREDERICK W. SCHIECK
ACTING ASSISTANT ADMINISTRATOR
BUREAU FOR LATIN AMERICA AND THE CARIBBEAN
AGENCY FOR INTERNATIONAL DEVELOPMENT
BEFORE THE
HOUSE APPROPRIATIONS SUBCOMMITTEE
ON FOREIGN OPERATIONS
MARCH 22, 1990

Mr. Chairman, members of the Subcommittee, thank you for the opportunity to share with you A.I.D.'s perspective on the remarkable changes underway in Latin America and the Caribbean, and in Central America particularly. I also want to comment briefly on our proposed economic assistance program for the countries of the region.

Sweeping changes are taking place in our world today. We are particularly thrilled with the events transpiring in own our hemisphere. In Panama, democracy is taking hold in a country that had suffered under more than two decades of authoritarian rule. In Nicaragua, free and fair elections mark a critical step toward peace and democracy in that strife-torn country. In Chile, a new democratically-elected president has just recently been sworn into office, marking the end to 17-years of authoritarian rule. And in Haiti, profound changes are underway, with a new interim civilian government and the prospects of fair and open elections in a few months. Every nation in our hemisphere has now embraced, or is moving toward economic, social and political freedoms, except for the lone, isolated country of Cuba. Who could have imagined such a picture a year ago, or even four months ago?

It is an exciting time to be working in the LAC region. The reality of a free, democratic and stable hemisphere is closer than ever before. As the President has repeatedly stated, "the day of the dictator is over." We at A.I.D. look forward to working with this Subcommittee and the rest of Congress on the important agenda before us.

A.I.D. STRATEGY AND OVERALL OBJECTIVES

The consolidation of democracy in the 1990's will have to see an economic transformation of Latin America as profound as the political transformation of the 1980's. It is plainly in our national interest to support the efforts of our neighbors to build a future based on economic freedom as well as political freedom, a future that fulfills the promise of democratic institutions and individual opportunity to satisfy the needs and aspirations of all Americans.

We must continue to encourage broadly-based, sustainable economic growth. There is a fundamental relationship between democratic freedoms and economic opportunity: they sustain one another. Fragile democracies are reinforced by sustained economic growth and opportunity. And open societies encourage the creativity and entrepreneurship essential to economic success.

In order to facilitate broadly-based, sustainable economic growth in the hemisphere, A.I.D. encourages the following mutually reinforcing objectives: (1) the adoption of and continued adherence to economic policies that promote investment in labor-intensive, export-oriented private sector activities that increase real per capita income; (2) a vigorous response by the private sector to a favorable policy environment; (3) the acceleration of opportunities for increased participation in the economy by the historically disadvantaged; and (4) the preservation and sustainable use of the natural resource base.

The countries in the region, particularly the nascent democracies, also need effective democratic institutions and competent civilian government. Another component of A.I.D.'s overall strategy, therefore, is to support the evolution of stable, democratic societies through an emphasis on strengthening democratic institutions, the rule of law, and respect for civil and political rights.

Within this context, A.I.D. is beginning to provide assistance to governments in restructuring the public sector. Our efforts focus on support for decentralization and modernization of governmental structures and procedures, privatization of state enterprises, improved financial management and accountability, and improved efficiency to provide essential services.

NEW INITIATIVES

Before I turn to the core Administration request for assistance to Latin America and the Caribbean for FY 1991, I would like to discuss several new initiatives in the region. First, we seek $500 million in Supplemental FY 1990 funds to support Panama's economic recovery. Second, we seek $300 million in Supplemental FY 1990 funds to support the Chamorro Government's program to stabilize and reconstruct the Nicaraguan economy. And, third, we have requested $175 million in FY 1991 funds to support the President's new Andean Narcotics Initiative.

Panama and Nicaragua

While the President has combined the assistance request for Panama and Nicaragua into the same supplemental package, the problems and the solutions for these two countries are quite different. One important lesson that we have learned over the years in our development experience is that each country in which we work has its own set of political, social and economic problems. These problems require appropriate, and often unique, solutions. Therefore, even though a country's development can be supported in important ways by programs of regional cooperation, each country needs to be addressed individually.

Although the needs in both Panama and Nicaragua are large, these two countries face quite different problems, requiring different solutions.

Panama is a middle-income country, with a largely urban population. It has a long tradition of broad access to education and health services. Infant mortality is far lower than in most of Latin America, and literacy is close to universal. The current severe recession has primarily hurt people in urban areas due to unemployment. Rural areas have been much less affected by U.S. sanctions and looting. The country's fundamental immediate need is for a "jump start" that will restore confidence and get people back to work.

Over the longer term, the country also needs better economic policies, such as the elimination of numerous monopolies and special privileges, and the improvement in efficiency of delivery of government services. Such policy improvements will make possible more rapid economic growth, with increases in incomes and productive employment, and will facilitate the consolidation of stable democracy.

The Endara Government has committed itself to take the necessary policy actions, and our assistance will be linked to progress in these areas. Economic recovery can be expected within 1-2 years, although some changes -- strengthening democratic processes, improving public administration -- will take longer.

Nicaragua, on the other hand, is an economic basket case. It was much poorer than Panama when the Sandinista Government took over, and has fallen further behind both Panama and the rest of the hemisphere. Per capita GDP has fallen by almost 50 percent since 1978, and is now around $300 -- one of the lowest in the hemisphere. Inflation rates have been in excess of 100 percent for the past five years and over 10,000 percent for the past two. Loss of buying power and consumption has surpassed 70 percent.

Infant mortality and illiteracy are far too high. Bringing them down to Panama's level will be a long-term task. The entire productive structure -- far more concentrated in agriculture than in Panama -- has been severely damaged.

Recuperation will be slow, and will be dependent on successful implementation of a sequence of policy actions by the government: ending the hyperinflation, eliminating a plethora of "command economy" regulations, demobilizing the massive army, encouraging farmers to go back and replant, and finding a way to recreate flexible means for supplying agricultural inputs and increasing access to market opportunities. The country's economic recovery and achievement of sustainable growth will take 5-10 years of hard work.

For Panama, our strategy is to help the Endara Government stabilize the economy and rebuild a basis for renewed, sustainable growth. The new government has already made real and substantial achievements to date, in part because of the immediate assistance we made available. In order to help Panama continue to consolidate and expand its economic recovery, we believe that a one-time influx of assistance on the magnitude that we have requested is the most prudent course of action. Assuming our program is implemented promptly, we do not foresee a need for continuing, multi-year, substantial aid flows.

Our strategy in Nicaragua is quite different. A full and immediate turnaround in the economy is not realistic. The economic reconstruction needed will take several years to accomplish. Once immediate recovery measures take hold, U.S. assistance will be needed to support the new government's efforts to restructure the economy and the public sector, to reinvigorate private initiative and to ensure that the benefits of development are widely shared.

In both cases, prompt approval of the assistance package is of critical importance. Even though A.I.D. has signed agreements to disburse the immediate $42 million that was authorized by Congress for Panama, the second phase of assistance is desparately needed to prevent the loss of private sector confidence in the new government and to encourage IFI and third country assistance to Panama. And in Nicaragua, if the new government does not demonstrate economic gains early on, the government will be weakened -- to the detriment of democratization and the Nicaraguan people. I urge immediate action on the supplemental request.

Andean Narcotics Initiative

This year, the Administration will begin implementing President Bush's Andean Narcotics Initiative, a comprehensive attempt to reduce the production of cocaine in Colombia, Peru, and Bolivia. It combines military assistance to strengthen host-country law enforcement and interdiction capacity, with substantial additional narcotics-related economic assistance to become available starting in FY 1991. The latter, in the amount of $175 million, will be used to cushion the macroeconomic effect on Peru, Bolivia, and Colombia of reduced foreign exchange inflows, to finance alternative development activities in rural areas, and to increase jobs, income and foreign exchange earnings throughout the economy. Sustained law enforcement and interdiction programs are key to driving down the price paid to farmers for coca-leaf. Unless this happens, alternative development and income-substitution programs will have little appeal for the small coca-leaf producer. Under the President's Andean initiative, Peru, Bolivia, and Colombia are eligible to receive additional assistance if these countries can demonstrate adequate anti-narcotics performance and have sound economic policies for use of this assistance.

A.I.D.'s anti-narcotics financing will also include support for drug awareness and prevention programs. Narcotics addiction is increasingly a domestic problem in Peru, Colombia, and Bolivia. Working with private and public agencies, A.I.D.

has helped to create a greater public awareness of the dimensions of the domestic problem and the harmful effects of drug production, trafficking, and addiction on these countries' own societies. In addition, A.I.D. will support administration of justice improvements. For example, in Colombia, assistance will include court administration, training, and commodities which will help with a more efficient processing of narcotics cases.

FY 1991 REQUEST

Now turning to our core FY 1991 budget request, we are proposing a program level of $1.478 billion in ESF, DA and P.L. 480 resources to support a strategy for achieving sustainable economic, social and political progress in the LAC region. Of this total, $828.8 million (56.1%) is for Central America, including the $200 million for Nicaragua; $214.3 million (14.5%) is for the Caribbean; $334.3 million (22.6%) is for South America; and $75.5 million (5.1%) is for LAC Regional programs, of which $30.5 million is for regional programs in Central America.

A.I.D. is requesting $851.9 million in ESF primarily for policy reform to support economic recovery and growth. This amount includes $175 million for the President's Andean Narcotics Initiative and $200 million for Nicaragua. This level is essential for achieving minimum acceptable progress toward sustainable economic growth. ESF also will finance continuing democratic development initiatives in such areas as election assistance, legislative management, journalism and leadership development. Country-specific Administration of Justice programs, including activities being initiated in Argentina and Chile, are planned for nine LAC countries.

The FY 1991 DA budget request for Latin America and the Caribbean is $374.6 million. Of this amount, $50 million is for performance based programming within the region. Country-level allocations of $25 million have already been made to countries performing well, and the remaining $25 million is requested as a fund to be allocated later on the basis of good country performance and attractive policy reform-based projects.

For P.L. 480, A.I.D. is requesting $251.4 million for the LAC region, consisting of $184.0 million in Title I/III and $67.4 million in Title II. The levels reflect projected shortages in grain production, anticipated increases in the price of wheat, and foreign exchange limitations.

Mr Chairman, I would now like to briefly highlight some specific areas which I know are of interest to the Subcommittee.

EL SALVADOR

The recent success of the elections in Nicaragua makes it all the more urgent that peace return to El Salvador. As President Bush and Secretary of State Baker have stated, this is the year to end the war in El Salvador.

The ten-year-old Marxist-Leninist insurgency has devastated El Salvador's economic and social fabric. Since 1979, an estimated 70,000 Salvadorans have been killed, some 500,000 people have been displaced, and perhaps a million persons have migrated to other countries. The estimated cost of destroyed infrastructure and lost production to date is close to $2.6 billion. The adverse impacts of terrorist damage to the economy have been compounded by the devasting 1986 San Salvador earthquake and by declining prices for the country's major exports, especially coffee.

There has been progress, however. A major step was the peaceful transfer of power in June 1989 to the opposition party. The new President quickly initiated an ambitious, far-reaching economic reform program, reiterated support for improved agrarian reform, and entered into talks with insurgent groups. However, the November 11 rebel offensive has caused readjustment in some government program targets and interruptions in normal A.I.D. activities.

To address growing economic structural problems, the new Cristiani Government has begun applying strong and difficult economic remedies. These have included the areas of exchange-rate management, interest rates, foreign-trade liberalization, coffee marketing, banking (movement toward privatization), and government revenues. The Government of El Salvador also has announced an accompanying social program to help cushion the economic program's short-term adverse impact on the poor.

A.I.D.'s assistance has been instrumental in getting assistance to the poor. Agriculture programs have supported the agrarian reform. That reform has directly benefited over 525,000 persons (farmers and families), or about one-fifth of the rural poor. The target group is being broadened to include non-reform small farmers.

A.I.D's Health System Support project is strengthening the capability of the Ministry of Health to deliver and support basic health services, including preventative and primary care services important to the Ministry's child survival program. This program has contributed to a decline in infant mortality from 65 per 1,000 live births in 1985 to 50 in 1988.

The Education System Revitalization project has resulted in: the construction or reconstruction of 2,800 primary school classrooms which accommodate some 200,000 children; the provision of over 4 million textbooks throughout the country; the training of over 2,000 teachers and regional directors; and the establishment of a national maintenance system in which teachers, students, and community members participate (to date, the project has provided tool kits and training to 2,390 communities).

A.I.D. programs have provided credit to some 24,000 small and micro-enterprises in El Salvador. Other programs, while not directly targeting the poor, benefit them in the most direct and positive way, through job generation. For example, programs aimed at export development have generated an estimated 13,000 direct, sustainable jobs since 1986.

In addition to working to ensure that the needs of the poor are addressed, the Administration has been concerned about the problems in El Salvador's justice system. Our support has helped to strengthen the ability of the Government of El Salvador to bring cases like the Jesuits murder to trial by (1) continuing to stress with all levels of government the importance of human rights, especially the right to hold and express political views without fear of retaliation; and (2) by developing and strengthening institutions responsible for assuring that grievious violations of the law will be punished no matter who commits them.

I believe the Jesuits case shows that we are making inroads in this regard. One of President Cristiani's first acts after learning of the murders was to charge the A.I.D.-supported Special Investigations Unit (SIU) with leading the investigation of the case. He showed remarkable political will and courage in his public announcement that elements of the military were involved in the November 16 murders.

The SIU has been credited with the success of the investigation to date. U.S. forensic specialists who assisted the SIU have reviewed the Unit's work and found it professional and of very high quality--a capacity that did not exist prior to the A.I.D. Judicial Reform project.

We are also beginning to see progress in the enactment of legislation that protects the rights of the individual and strengthens the judicial system. For example, the establishment of a National Council for the Judiciary to propose judicial candidates for appointment by the Supreme Court will decrease the political nature of the judiciary and increase its independence from other government branches.

We are also addressing a host of other impediments to an effective judicial system, such as training for judicial personnel; access to laws; public education as to rights of individuals under the law; and coordination among the organizations responsible for investigation, prosecution, and decision. Reformers within El Salvador are enthusiastic in their support of the program and are making headway in improving a system which was never strong and is faced with extraordinary demands.

As presented in our FY 1991 Congressional Presentation, A.I.D. believes that U.S. economic assistance is critical to El Salvador's success in achieving social and economic reforms in the face of the insurgency. To reduce or eliminate assistance, as some have suggested, would send a wrong signal and would be highly counterproductive. The social and economic situation and level of assistance will have a direct bearing on the ability of the Cristiani Administration to negotiate on a level playing field with the FMLN. This ability would be sharply undermined if, while undertaking a dialogue with the insurgents, the domestic economic situation became unstable or overly contentious in political terms.

In human terms, a worse economic situation will mean sharp cuts in consumption and a delay in private sector investment. Most worrisome, cuts in public sector expenditures would result in cuts in the investment budget and a reduced ability of the Government of El Salvador to fund programs to improve the quality of life of the country's population, especially the poor majority who benefit directly and indirectly from U.S. economic assistance.

Turning to the rest of Central America, we see a strengthening of the democratic process and strong economic growth, underpinned by economic policy reform measures. Within a year, Costa Rica, Honduras, and Guatemala will each have new democratically elected governments in place. Economic reform programs in Costa Rica and Guatemala are generating strong economic growth, and new economic reform programs in Honduras sharply improve the prospects of recovery of that nation's economy. Our assistance is critical in strengthening this democratic process and economic growth, benefitting the people.

CARIBBEAN REGION

Several Members have expressed concern about the lower support levels for the Caribbean in FY 1990. Unfortunately due to the combination of earmarks and a reduced level of overall assistance, several countries in the region, particularly in the Caribbean, are not receiving the level of assistance that they need. Compared to FY 1989, when the Caribbean region received $207.1 million in new obligations (excluding hurricane assistance), the FY 1990 level has fallen 23.6% to an estimated $158.2 million. Secretary of State Baker has expressed concern on several occasions about the lower levels of ESF assistance to the Caribbean, where our budget request level of $60 million was reduced to only $5.974 million.

In FY 1991, we hope to correct this problem. Our FY 1991 request level of $214.3 million is 35.5% higher than the FY 1990 level, and is 3.4% higher than the FY 1989 level. We believe that this level reflects the minimum requirement necessary to ensure that U.S. national interests of sustained economic growth, political stability, and respect for human rights are met in the Caribbean. We must continue to encourage open trade, freedom, and cooperation with our efforts to curtail shipment of narcotics through the region.

Mr. Chairman, I realize that you and the members of this Subcommittee are sensitive to this problem. I appreciate the efforts that you made last year to try to limit the practice of earmarking. I am optimistic that we will be able to work out a solution this year that will give us the ability and flexibility to meet the needs of our neighbors in the Caribbean as well as the rest of this hemisphere.

HAITI

We are pleased with the recent events in Haiti. Lt. Gen. Prosper Avril's departure and the installation of a provisional civilian president are encouraging signs that democracy may be established soon in Haiti. There are good prospects that fair and open elections will take place in three to six months. Assuming that events proceed without serious setbacks, external assistance to the electoral process will be necessary. There remains $500,000 of Haitian government-owned local currency from previous year programs which could help defray the costs of elections.

We are hopeful that a democratic transition will take place and that the Haitian people will achieve social, political and economic freedoms. As these events unfold, Haiti's need for additional assistance will have to be considered carefully.

CONCLUSION

While I have highlighted only a few of our country and program initiatives, I cannot stress enough the importance of the challenge facing us throughout our entire hemisphere. Yes, significant strides have been made -- due in a large part to the success of our past support and leadership. But the balance of the forces of democracy, prosperity and stability is still fragile. We need to invest in the future to influence the transition in Latin America and the Caribbean, and to insure the sustainability of these forces. With open markets and freedom, both the United States and our neighbors benefit.

Thank you. I will be glad to respond to any questions.

Mr. OBEY. Thank you.

Let me simply make one observation in response to one thing you said. With respect to the Caribbean, I frankly think that I was doublecrossed by the Administration with respect to one item. I was asked by the Administration to keep earmarks off to the greatest extent possible. Mr. Edwards and I tried to do that.

I dissuaded one member of this subcommittee from earmarking $5 million for hurricane relief in the Caribbean because I was told the Administration intended to do that anyway, so we should not just add to the earmarking level. We kept the earmark off and they did not provide the money. I do not think we were dealt squarely with on that point. We are going to do something about that in the supplemental, I guarantee you.

Mr. Rowan.

MR. ROWAN'S OPENING STATEMENT

Mr. ROWAN. Mr. Chairman, I too will keep it brief. I have a longer statement.

There is good news and not so good news, or at least not total success, I want to underscore. The good news, that progress has been impressive: the changes in Haiti, Chile, Panama, Nicaragua, Colombia, where the government has undertaken a major campaign against narco-traffickers and made some important gains.

But the situation is by no means settled in many of these countries. General Pinochet is still the head of the military in Chile. In Panama, the Endara government is struggling to retrain and reorient its security force in a country faced with crime and internal unrest and narcotrafficking patterns established under the Noriega regime.

In Nicaragua, it is not clear that the Sandinistas will fully give up control of the military and internal security police force. In Colombia, most of the major drug lords are fugitives, but continue in business.

Specifically, our security assistance request for fiscal year 1991 reflects our interest in dealing with these remaining problems: regional peace, the democratization process, the protection of human rights, and the counter-narcotics programs in the western hemisphere.

This is not the time, apropos of your comments on El Salvador, which I concur with and I think are very sensible, but this is not the time to stop our security assistance to young democracies that are struggling. In El Salvador, the FMLN continues to attack a democratically elected government. Perhaps we are on the verge of serious negotiations. Let us hope so.

But the most important leverage that the Cristiani government has in negotiating for a political settlement is our security assistance effort, the support from the United States. It also provides Cristiani with the political strength to counter pressure from the right wing.

In Honduras, our military assistance has to be looked at in a regional context. Honduras has been our strongest ally in the region and we have made a commitment to help them modernize their armed forces. And this fiscal year 1991 request for $40 million brings them closer to that goal. We believe that a small but strong Honduran military would be a positive contributor to regional stability.

Nearby, Guatemala faces persistent threats from an ongoing insurgency and from right-wing extremists, both of which aim to overthrow the elected civilian government. Our security assistance proposal, which provides only non-lethal aid, is a force for positive change within the government, the military, and society, we believe.

The Andean countries together face the problems of narcotics, as well as of course domestic instability. In Peru, the Upper Huallaga Valley accounts for 60 percent of the coca leaf production. In Colombia, the drug traffickers have declared war against the government and killed numerous officials. In Bolivia, the illegal production of coca leaf remains the country's biggest challenge. Our Andean counternarcotics initiative is supported by this $137 million requested for these three countries.

Finally, I would say that, given the changes in Soviet policy, reduced support in the region, plus the change in Nicaragua, leaves these insurgent groups facing the prospect of reduced support. We do not know if they will give up the struggle, as the M-19 did two weeks ago in Colombia, or continue it or seek some kind of political compromise or become even more violent.

An important factor here is Cuba, which has played a key role in providing aid to insurgencies in the region. Cuba's own situation is likely to worsen, given probable cuts in Soviet aid. But we do not know how quickly this will lead to reduced support for subversion.

In any case, we need to keep up the pressure on the insurgents while the democratically elected governments continue to offer peaceful solutions.

We will continue to be insistent in our support of democratic institutions, human rights and civil liberties. For example, in El Salvador we have insisted that the murderers of the six Jesuit priests face justice and they are awaiting trial.

To protest recent human rights abuses in Guatemala, the Ambassador was recalled to Washington recently to register our deep concern, and he was instructed to return to Guatemala and deliver messages from the highest level of the U.S. government reiterating our insistence on respect for human rights.

Mr. Chairman, there is a lot more that remains to be done in this hemisphere on the security front and we ask your help in this regard in the coming months.

Thank you.

[The prepared statement of W. Rowan follows:]

Embargoed until delivery, 1000/22 March, 1990

STATEMENT OF
ASSISTANT SECRETARY OF DEFENSE FOR INTERNATIONAL SECURITY AFFAIRS
HENRY ROWEN
HOUSE APPROPRIATIONS SUBCOMMITTEE ON FOREIGN OPERATIONS
22 MARCH 1990

MR. CHAIRMAN, THANK YOU FOR THE OPPORTUNITY TO BE HERE TODAY TO TESTIFY ON ISSUES OF CONCERN IN THE WESTERN HEMISPHERE. I LOOK FORWARD TO WORKING WITH MEMBERS OF THIS COMMITTEE DURING THE COMING MONTHS.

THE LAST TWELVE MONTHS HAVE SEEN TREMENDOUS POLITICAL AND SOCIAL CHANGES THE WORLD OVER, INCLUDING THE WESTERN HEMISPHERE. IN HAITI, GENERAL AVRIL, HAS BEEN FORCED OUT OF OFFICE. IN CHILE, GENERAL PINOCHET HAS TURNED OVER THE REINS OF GOVERNMENT TO THE DEMOCRATICALLY ELECTED PATRICIO AYLWIN. IN PANAMA, THE ENDARA GOVERNMENT IS CONSOLIDATING ITS POSITION AND THE FORMER DICTATOR, GENERAL NORIEGA, IS IN JAIL IN THE U.S. IN NICARAGUA, THE SANDINISTAS LOST THE ELECTION AND THE WINNER, MRS. CHAMORRO, IS FORMING A CABINET IN ANTICIPATION OF HER INAUGURATION NEXT MONTH. IN COLOMBIA, THE GOVERNMENT HAS UNDERTAKEN A MAJOR CAMPAIGN AGAINST NARCO-TRAFFICKERS AND HAS MADE SOME IMPORTANT GAINS.

HOWEVER, THE SITUATION IS BY NO MEANS SETTLED IN MANY OF THESE COUNTRIES. GENERAL PINOCHET IS STILL HEAD OF THE MILITARY IN CHILE. IN PANAMA, THE ENDARA GOVERNMENT IS STRUGGLING TO RETRAIN AND REORIENT A SECURITY FORCE IN A COUNTRY FACED WITH CRIME, INTERNAL UNREST AND NARCOTRAFFICKING PATTERNS ESTABLISHED UNDER THE NORIEGA REGIME. IN NICARAGUA, IT IS STILL UNCLEAR IF THE SANDINISTAS WILL FULLY GIVE UP CONTROL OF THE MILITARY AND THE INTERNAL SECURITY POLICE FORCE. IN COLOMBIA, MOST OF THE MAJOR DRUG LORDS ARE FUGITIVES BUT CONTINUE TO DO BUSINESS.

MR. CHAIRMAN, ALL THIS DEMONSTRATES THAT EVEN THOUGH THERE HAS BEEN TREMENDOUS PROGRESS TOWARD DEMOCRACY IN THE REGION, THE JOB HAS ONLY BEGUN. WE HAVE A LONG WAY TO GO TO INSURE THAT OUR GOALS ARE MET.

WE, AT DOD, BELIEVE THAT OUR APPROACH AT THIS POINT MUST BE RESPONSIVE, STEADFAST, AND INSISTENT. RESPONSIVE TO THE CHANGES THAT HAVE TAKEN PLACE. STEADFAST IN OUR SUPPORT TO DEMOCRATIC GOVERNMENTS IN THEIR FIGHT AGAINST THE VIOLENCE OF INSURGENTS AND DRUG KINGPINS. AND INSISTENT IN OUR DEMAND FOR PROGRESS IN DEMOCRATIZATION AND HUMAN RIGHTS. OUR SECURITY ASSISTANCE REQUEST FOR FISCAL YEAR 1991 REFLECTS OUR INTERESTS IN REGIONAL PEACE, THE DEMOCRATIZATION PROCESS, THE PROTECTION OF HUMAN RIGHTS, AND THE COUNTER-NARCOTICS PROGRAMS IN THE WESTERN HEMISPHERE.

MR. CHAIRMAN, THE U.S., UNDER A BIPARTISAN AGREEMENT, HAS RESPONDED SWIFTLY TO RECENT CHANGES IN THE WESTERN HEMISPHERE. WITHIN FOUR WEEKS AFTER NORIEGA'S REMOVAL, THE ADMINISTRATION OFFERED 500 MILLION DOLLARS TO SUPPORT PANAMA. LESS THAN THREE WEEKS AFTER THE ELECTION IN NICARAGUA, THE PRESIDENT LIFTED ECONOMIC SANCTIONS AND REQUESTED 300 MILLION DOLLARS FROM THE DOD APPROPRIATION TO HELP MRS. CHAMORRO REBUILD A SHATTERED ECONOMY. AS YOU KNOW, THE PRESIDENT HAS DIRECTED MR.CHENEY AND MR. DARMAN TO NEGOTIATE THE DETAILS OF THIS PROGRAM WITH THE CONGRESSIONAL LEADERSHIP.

WE HAVE ALSO BEEN RESPONSIVE AT THE POLITICAL LEVEL; THE PRESENCE OF THE VICE PRESIDENT AT THE INAUGURATIONS OF THE PRESIDENTS OF CHILE AND BRAZIL DEMONSTRATES OUR STRONG INTEREST IN THESE POSITIVE POLITICAL DEVELOPMENTS.

DESPITE THESE FAVORABLE DEVELOPMENTS, THE VIOLENCE AND WAR BROUGHT BY INSURGENCIES AND NARCOTICS CARTELS CONTINUES; THEREFORE, THIS IS NOT THE TIME TO STOP OUR SECURITY ASSISTANCE TO THESE YOUNG DEMOCRACIES. IN EL SALVADOR, THE FMLN CONTINUES TO ATTACK A DEMOCRATICALLY ELECTED GOVERNMENT. WE BELIEVE THAT CONTINUED U.S. MILITARY ASSISTANCE TO THE CRISTIANI GOVERNMENT IS ITS MOST IMPORTANT LEVERAGE IN NEGOTIATING FOR A POLITICAL SETTLEMENT WITH THE REBELS. EQUALLY IMPORTANT, OUR ASSISTANCE PROVIDES CRISTIANI THE NEEDED POLITICAL STRENGTH TO COUNTER PRESSURE FROM THE RIGHT WING EXTREMISTS. IN HONDURAS, U.S. MILITARY ASSISTANCE MUST BE CONSIDERED IN A REGIONAL CONTEXT. HONDURAS HAS BEEN OUR STAUNCHEST ALLY IN THE REGION, AND WE HAVE MADE A COMMITMENT TO HELP THEM MODERNIZE THEIR PROFESSIONAL ARMED FORCES. THE FY91 REQUEST OF 40 MILLION DOLLARS BRINGS THEM CLOSER TO THAT GOAL. WE BELIEVE THAT A SMALL BUT STRONG HONDURAN MILITARY WILL BE A POSITIVE CONTRIBUTOR TO REGIONAL STABILITY. NEARBY, GUATEMALA FACES PERSISTENT THREATS FROM AN ONGOING INSURGENCY AND FROM RIGHT WING EXTREMISTS, BOTH OF WHICH AIM TO OVERTHROW THE ELECTED CIVILIAN GOVERNMENT. OUR SECURITY ASSISTANCE, WHICH PROVIDES ONLY NON-LETHAL AID, HAS BEEN A FORCE

FOR POSITIVE CHANGE WITHIN THE GOVERNMENT, THE MILITARY AND THE SOCIETY.

THE ANDEAN COUNTRIES TOGETHER FACE THE PROBLEM OF NARCOTICS. IN PERU, THE UPPER HUALLAGA VALLEY ACCOUNTS FOR SIXTY PERCENT OF ALL COCA LEAF PRODUCTION. IN COLOMBIA, THE DRUG TRAFFICKERS HAVE DECLARED WAR AGAINST THE GOVERNMENT AND KILLED NUMEROUS OFFICIALS. IN BOLIVIA, THE ILLEGAL PRODUCTION OF COCA LEAF REMAINS THE COUNTRY'S BIGGEST CHALLENGE. THE U.S. ANDEAN COUNTER-NARCOTICS INITIATIVE IS SUPPORTED BY THE 137 MILLION DOLLARS REQUESTED FOR THESE THREE COUNTRIES.

GIVEN THE SOVIETS' PLEDGE TO DISCONTINUE ASSISTANCE AND THE RECENT DEFEAT OF THE SANDINISTAS AT THE VOTING BOOTH, THE INSURGENT GROUPS ARE FACING THE PROSPECT OF REDUCED SUPPORT. WE DON'T KNOW WHETHER THEY WILL GIVE UP THE STRUGGLE, AS THE M-19 GROUP DID IN COLOMBIA TWO WEEKS AGO, AND SEEK SOME KIND OF POLITICAL COMPROMISE, OR BECOME EVEN MORE VIOLENT IN DESPERATION. AN IMPORTANT FACTOR IS CUBA. IT HAS PLAYED A KEY ROLE IN PROVIDING AID TO INSURGENCY MOVEMENTS. WHILE CUBA'S SITUATION WILL LIKELY WORSEN DUE TO PROBABLE CUTS IN SOVIET AID, WE DO NOT KNOW HOW QUICKLY THIS WILL LEAD TO REDUCED SUPPORT FOR SUBVERSION. IN ANY CASE, WE MUST KEEP UP THE PRESSURE ON THE INSURGENTS WHILE THE DEMOCRATICALLY ELECTED GOVERNMENTS CONTINUE TO OFFER PEACEFUL POLITICAL SOLUTIONS.

WE WILL ALSO BE INSISTENT IN OUR SUPPORT OF DEMOCRATIC INSTITUTIONS, HUMAN RIGHTS AND CIVIL LIBERTIES. THE MESSAGE IS THAT WHILE WE WILL CONTINUE TO PROVIDE SECURITY ASSISTANCE, WE DEMAND IMPROVEMENT IN HUMAN RIGHTS AND DEMOCRATIC PRACTICES IN THESE COUNTRIES. WE INSISTED THAT THE MURDERERS OF SIX JESUIT PRIESTS FACE JUSTICE IN EL SALVADOR, AND THEY ARE AWAITING TRIAL. TO PROTEST RECENT HUMAN RIGHTS ABUSES IN GUATEMALA, WE RECALLED OUR AMBASSADOR TO WASHINGTON FOR CONSULTATIONS. HE WAS INSTRUCTED TO RETURN TO GUATEMALA AND DELIVER MESSAGES FROM THE HIGHEST LEVELS OF THE U.S. GOVERNMENT REITERATING OUR INSISTENCE ON RESPECT FOR HUMAN RIGHTS.

WITH REGARD TO DEMOCRACY IN NICARAGUA, WE WILL CONTINUE TO ENCOURAGE MR. ORTEGA TO PEACEFULLY TURN OVER POWER TO PRESIDENT-ELECT CHAMORRO, AND WE WILL ASSIST HER IN BUILDING DEMOCRATIC POLITICAL INSTITUTIONS.

MR. CHAIRMAN, WE ARE CONCERNED FOR THE STABILITY AND SECURITY OF THESE NEIGHBORING COUNTRIES FOR MANY REASONS, INCLUDING THE POSSIBILITY THAT THEIR PROBLEMS TODAY MIGHT BECOME OUR OWN TOMORROW; FOR THAT VERY REASON, WE CARE FOR BASIC HUMAN RIGHTS AND CIVIL LIBERTIES THERE.

COLOMBIA

COLOMBIA IS AT THE FOREFRONT OF THE LATIN AMERICAN COUNTER-NARCOTICS WAR AND REMAINS OUR STRONG ALLY IN THIS ARENA. SINCE

THE AUGUST ASSASSINATION OF COLOMBIAN PRESIDENTIAL CANDIDATE GALAN AND THE INFUSION OF $65 MILLION IN 506(A) EMERGENCY MILITARY ASSISTANCE EQUIPMENT AND TRAINING, COLOMBIA HAS AGGRESSIVELY PURSUED A COUNTRY WIDE EFFORT AGAINST THE COCAINE KINGPINS AND THEIR ESTABLISHMENTS. ROUNDING OUT THE EQUIPPING OF THE COLOMBIAN MILITARY AND POLICE THIS YEAR WAS THE PROVISION OF $80 MILLION OF HELICOPTERS AND REPAIR PARTS PURCHASED BY THE COLOMBIANS UNDER AN EXIM BANK GUARANTEED LOAN. OUR EFFORT IN THE FUTURE WILL BE TO MAINTAIN THE MOMENTUM OF COLOMBIA'S OPERATIONS AND TO FOCUS ON SUSTAINING THE EQUIPMENT WE HAVE PROVIDED. NOTWITHSTANDING THE RECENT AGREEMENT OF THE M-19 GUERRILLA GROUP TO LAY DOWN ITS ARMS, COLOMBIA CONTINUES TO SUFFER FROM THE LONG-STANDING THREATS OF OTHER INSURGENT GROUPS.

BOLIVIA

BOLIVIA, WHILE NOT SUFFERING FROM AN ACTIVE INSURGENCY, FACES THE PROBLEM OF AN EXPANDING NARCOTICS PRODUCTION. AS COUNTER-NARCOTICS ENFORCEMENT EFFORTS ACHIEVE GREATER EFFECTIVENESS IN COLOMBIA, WE ARE WITNESSING A SHIFTING OF COCAINE PRODUCTION ACTIVITY INTO BOLIVIA. THE GOVERNMENT OF BOLIVIA HAS RECENTLY AUTHORIZED THE PARTICIPATION OF THE ARMED FORCES IN COUNTER-NARCOTICS OPERATIONS IN AN EFFORT TO CONFRONT THIS PROBLEM. AS CONSULTATIONS WITH THE HOST GOVERNMENT CONTINUE, IT'S IMPORTANT TO CONTINUE OUR SUPPORT TO ENSURE A SUCCESSFUL LEVEL OF COOPERATION AMONG ALL COUNTERNARCOTICS FORCES IN THE REGION.

PERU

Peru has continued to participate in combined anti-narcotics programs administered by the U.S. government. Until this fiscal year, Peru has not received much security assistance support because of Brooke sanctions which prevent US assistance to debtor countries which fail more than one year in payment arrears. Peru's economy suffers from spiraling inflation (2500%) and plummeting economic activity. The Peruvian military in the past year has begun to recognize its greatest threat was from within its borders and not outside. The Shining Path insurgent group has coopted large segments of the peasant population and infests the primary coca growing region. Intensified efforts by the Peruvian military and police have had some success, however, the battle with insurgent groups is by no means won.

CARIBBEAN COUNTRIES

Over the past several years, programs for the island nations of the Eastern Caribbean have suffered because of the lack of funds available to support them. Jamaica, the Dominican Republic, and the smaller island nation states of the region are very vulnerable to drug smuggling operations. In the early 1980's, the U.S. along with the British helped establish the Regional Security System, or RSS, and provided patrol boats and other equipment useful for counter-narcotics activities. Now those

EQUIPMENT ARE DETERIORATING AND THEIR USE IS LIMITED BECAUSE OF INSUFFICIENT OPERATIONS AND MAINTENANCE FUNDS. THE $7.1 MILLION WE ARE REQUESTING IN FISCAL YEAR 1991 WILL HELP RESTORE THE VIABILITY OF THE PROGRAMS FOR THESE COUNTRIES.

CENTRAL AMERICAN PEACE ACCORD

DEMOCRATIZATION IN NICARAGUA IS JUST ONE FACET OF THE PEACE PLAN ORIGINALLY AGREED TO AT ESQUIPULAS, GUATEMALA IN 1988. MUCH MORE NEEDS TO BE DONE IN ORDER TO IMPLEMENT THE NEXT STEP IN THE PROCESS BY INSURING THE DISCONTINUATION OF ARMS TO THE GUERRILLA FORCES STILL FIGHTING IN EL SALVADOR AND GUATEMALA. THE SANDINISTAS HAVE SUPPLIED THE FMLN IN EL SALVADOR THROUGHOUT THE LONG HISTORY OF THAT STRUGGLE. THEY HAVE ALSO PROVIDED THE GUERRILLAS WITH A SAFE HAVEN, REAR OPERATING AND TRAINING AREA, AND A TRANSIT POINT FOR GUERRILLAS. EVEN THOUGH THE SANDINISTAS LOST THE RECENT ELECTION, THEY REMAIN A POTENT FORCE WHICH, WITH CONTINUED SUPPORT FROM CUBA, COULD CONTINUE CLANDESTINE SUPPORT FOR THE FMLN.

THE ONLY WAY TO INSURE THAT THE FOUR DEMOCRACIES WILL KEEP THE PRESSURE ON THE SANDINISTAS TO SURRENDER POWER AND NOT JUST THE TRAPPINGS OF GOVERNMENT TO MRS. CHAMORRO IS TO ASSURE THEM THAT THE U.S. STANDS BEHIND THEM AND WILL SUPPORT THEM IN THEIR EFFORTS TO FULLY IMPLEMENT THE PEACE AGREEMENT. THE SECURITY ASSISTANCE PROGRAMS FOR EL SALVADOR AND HONDURAS ARE CRITICAL TO THIS PROCESS. NEITHER COUNTRY HAS THE RESOURCES TO FIELD THE

NECESSARY MILITARY FORCES WHILE CARRYING OUT NEEDED REFORMS, MODERNIZATION, AND PROFESSIONAL DEVELOPMENT. SINCE THE CURRENT SITUATION IN CENTRAL AMERICA STARTED, HONDURAS HAS RELIED ON FORCE IMPROVEMENTS RATHER THAN FORCE EXPANSION TO MEET THE THREAT POSED BY INSTABILITY THROUGHOUT THE REGION. COMPLETION OF THIS PROCESS IS IMPORTANT NOT ONLY TO THE SECURITY OF HONDURAS BUT TO THE SECURITY AND STABILITY OF THE REGION.

MR. CHAIRMAN, EACH OF OUR COUNTRY REQUESTS FOR CENTRAL AMERICA IS A PART OF A WHOLE. EACH OF THESE DEVELOPING DEMOCRACIES DEPENDS ON THE OTHERS FOR REGIONAL STABILITY, FOR STRENGTH OF PURPOSE, AND FOR COHESIVENESS IN THE FACE OF CONTINUED GUERRILLA ATTACKS AND CUBAN INTIMIDATION. CONTINUED U.S. ECONOMIC, POLITICAL, AND MILITARY SUPPORT FOR THE REGION IS CRITICAL TODAY IF THESE COUNTRIES ARE TO SUCCESSFULLY HOLD THE SANDINISTAS TO THE PEACE ACCORD AND TO THE MANDATE OF THE NICARAGUAN PEOPLE.

AS THE SITUATION IN CENTRAL AMERICA SEEMS TO IMPROVE DAY BY DAY, WE BELIEVE THESE IMPROVEMENTS CAN BE TRACED DIRECTLY TO THE U.S. SUPPORT FOR THE PEACE PROCESS AND FOR THE BUILDING OF DEMOCRATIC INSTITUTIONS IN EACH OF THESE COUNTRIES. OUR REQUESTS FOR FISCAL YEAR 1991 CONTINUE THIS SUPPORT DURING WHAT WE HOPE TO BE A PERIOD OF TRANSITION TO FREELY ELECTED, DEMOCRATIC GOVERNMENTS AND THE END TO WAR, HUMAN RIGHTS ABUSE AND THE SCOURGE OF DRUGS THROUGHOUT THE REGION. THANK YOU.

Mr. OBEY. Mr. Lewis, let me skip you and pass on. Mr. Gallo.

ADMINISTRATION'S DRUG STRATEGY AND PROGRAMS

Mr. GALLO. Thank you, Mr. Chairman.

During a recent survey in my area, drugs is the number one concern, stripping away all other issues. The drug initiative that is taking place, as you mentioned, with the Colombians and also Mexico is very important. Maybe you could give me some indication, and the members of this committee, as to how successful it is and what elements are proving to be more successful than others?

One of the questions I am asked is why are we spending all of this money other places when we have individuals here that need rehabilitation and treatment? So if you would expand on that.

Mr. LEVITSKY. Certainly, Mr. Gallo. Let me point out that "spending all that money" is somewhat of an exaggeration. Out of the $10 billion that the President has requested for drug programs, Federal money that is, only about $500 million in terms of the kinds of programs we are talking about with overseas countries is involved here.

So that the bulk of this money is spent in the United States on law enforcement, on interdiction, on treatment, rehabilitation, education, and demand reduction, which of course is the heart. We want to get at the demand problem in this country so that it will not attract the supply as it comes in.

But as far as the effectiveness of our programs in Latin America, particularly with regard to crack cocaine, which is our biggest and most violent problem here, we have had a strategy, a comprehensive strategy, in this Administration since last September, and we issued another one in February, the President's strategy.

We have a comprehensive program that attacks the drug chain from the very primary level, that is the growth of the drug crops, through the production cycle, the distribution cycle, and then from our borders into this country, and combine it with an international effort that attacks money-laundering worldwide to separate the drug lords from their profits, chemical precursors and essential chemicals without which the drugs could not be produced, working with other countries.

What are the results? I think it is a little premature with regard to this strategy to look at what the results are. But if you look at what happened last year, we see a number of positive things, and again with an overlay of a lot of negative things happening, like corruption and ineffectiveness, that I mentioned in my statement.

But take a look at some of the things that have happened and they are quite positive. General Noriega is here behind bars. Panama has passed from a minus country on drugs to a plus country, with a lot of problems, and we are going to help them try to rebuild their forces that are fighting against drugs within Panama. We want Panama to be off-limits and so does that government.

Rodriguez Gacha is dead, one of the biggest traffickers. 14 Colombian major traffickers are in the United States behind bars. We gave about $65 million in assistance to the Colombian government to help them wage their very brave struggle against the traffickers, and we are going to be increasing our assistance, both law enforcement assistance, military assistance, and economic assistance, in 1991 to help them cope with the results of success, we hope, that is the dislocation of the cocaine trade.

A lot of cocaine was produced, but about 200 metric tons of cocaine, which is a huge amount, was seized in this hemisphere both by us and by governments like Colombia, 35 metric tons, and Mexico, more than 30 metric tons.

So our programs in assistance, and we assist these governments specifically in narcotics control and in some cases in military assistance, are having an effect. Have we solved the problem? No. Are we beginning to see some good progress? Yes.

DRUG PROGRAMS IN MEXICO

Mr. GALLO. Is the cooperation in Mexico much different than it has been in the past?

Mr. LEVITSKY. Well, I would say there has been a complete turnaround, particularly during the last year, in the Salinas Administration. And what we have found in our own programs with Mexico is a greater willingness, for example, to go after interdicting the cocaine coming into this country.

Some of this, unfortunately, is reflected in lower figures in eradication marijuana and opium crops, because they are using the air assets that we help them sustain, that is the helicopters, to transport troops and to make raids, which is consequently what you see is more traffickers being arrested and a lot more cocaine being interdicted and seized, with a lowering of the eradication campaign.

We want to try to do better on both sides. But the Mexican Administration under President Salinas has committed itself to fighting against drugs, not because we have asked them to, but because they see it as a national security threat. And from the drug control standpoint, that is the best situation you can have, that the political will and the determination of the government is involved. That is what you need to be able to work with them.

FY 91 REQUEST FOR NICARAGUA AND PANAMA

Mr. GALLO. Mr. Secretary, dealing with the supplemental—and I would agree it is important that we have an infusion of moneys available for Nicaragua and Panama, and I note the amount of money that you are looking for in the supplemental, but I also look at the 1991 budget and I do not see any dollars in there for Panama or Nicaragua.

With Nicaragua, I guess things changed rather quickly and maybe the budget reqeust would have been premature at that stage because nothing had taken place. But in view of the events that have taken place, is there a modification in the Administration's proposal dealing with both Panama and Nicaragua?

Mr. ARONSON. Yes, Congressman. When the President announced the supplemental last Tuesday, he also said that he intended to submit a budget amendment for the fiscal year 1991 budget to request an additional $220 million for Nicaragua. We have sent down an inter-agency economic team to the country. They first received Mrs. Chamorro's economic team. Now they are going down to Nicaragua, and they arrived yesterday, to make a more thoroughgoing assessment.

We will come back and report to the committee in terms of the specifics of that '91 request. But we are going to ask for that for Nicaragua.

I would just like to make one point. With regard to Panama, we believe and the Panamanian government believes that there is enough inherent vitality in that economy, which was in fact a strong and growing economy before the Noriega dictatorship drove it into the ground, that with this supplemental, if we can pass it in the dimensions that the President has requested, that essentially they can revive the private sector, re-establish their relationship with the international financial institutions, and begin to receive flows from the World Bank, the IDB, and the IMF, and essentially become economically self-sufficient.

They are not asking for and they do not foresee an long-term economic relationship. Nicaragua is a very different economy, as you know, and there we will be asking for an additional $200 million.

Mr. GALLO. Let me just add to that. I have had the opportunity of talking with individuals from Panama that made it very clear early on that they needed a quick infusion in the small business area and were asking that those moneys not be directed per se to the Panamanian government, but directly to the small business community.

Just recently I got a report that that is happening, so I want to compliment you. And I thank you for your comment.

Thank you, Mr. Chairman.

Mr. OBEY. Thank you.

Mr. Coleman.

DEBT OF LATIN AMERICAN COUNTRIES

Mr. COLEMAN. Thank you, Mr. Chairman. I apologize for being a little late. I had a conflicting subcommittee meeting. I am concerned with some of the same issues, however, that I know that we have talked about in this subcommittee, specifically the budgetary problems. How are we going to resolve some of these problems with no money? I mean, whether it is a supplemental or whatever it may be, it is money that our country determines we are going to borrow in order to take care of these problems.

I wanted to ask you, if you would not mind, to give us a country-by-country statement for the record concerning foreign indebtedness. I noticed in your statement, Mr. Secretary, you pointed out that foreign indebtedness remains a major stumbling block to growth, and I am sure you are referring to all the countries in this hemisphere. You may have enumerated specific ones in other points you made.

Your statement said: "Progress has been made, especially this past year, under the Brady Plan in reducing the region's external debt." I would be very interested to know, country-by-country, what the effect on their external debt has been, regardless of the Brady Plan.

I think some of that statement may be a little too general, overreaching perhaps. But I nonetheless would appreciate seeing it. I understand Costa Rica and Mexico certainly have been favorably affected by the Brady Plan. But I would also like to see your analysis of the foreign debt of Brazil and the other countries in the hemisphere.

You went on and referred to Venezuela and their debt reduction agreement. If you could just do this for us on a country by country basis, as kind of an update, you know. We will label it "circa 1990 or '89", whichever numbers are available that are the most recent. This will give us some estimate of where we are headed.

The reason I ask is that I think it is going to be valuable over the next several years to see if progress really has been made.

I also take from your statement the importance of the countries undertaking their own economic reforms, certainly. But I think that it would also be beneficial for us to see where they are not making progress. Then we can attribute whatever reasons we want to those shortcomings, whether it is their own failure to begin economic reform or our efforts not being strong enough.

Mr. ARONSON. Congressman, I will submit to you later in writing the specifics in terms of both the official and commercial debt of every country in the hemisphere.

[The information follows:]

See attached table, which provides a country-by-country breakdown which includes, among other data items, total external debt, medium/long term debt, external debt owed to private (commercial) lenders, and debt owed to official lenders (bilateral official and debt owed to multilateral financial institutions).

Attachment: "Official Debt in Latin America and the Caribbean: 1988."

Table 1

OFFICIAL DEBT IN LATIN AMERICA AND THE CARIBBEAN: 1988

$ million

	M/L FOREIGN DEBT	Private Lenders	Official Lenders	Official M/L as % of Total	MDB Official	Bilateral Official	Bilateral Official as % of Total	USG Long-term Loans & Credits	USG as % of Total	USE OF IMF CREDIT *	Official M/L Debt Plus IMF	as % of total	SHORT-TERM DEBT	TOTAL FOREIGN DEBT
LATIN AMERICA AND THE CARIBBEAN	366,576	235,261	99,678	23.3%	50,594	49,084	49.2%	11,908	2.8%	16,376	116,054	27.1%	44,511	427,463
ARGENTINA	48,166	39,406	8,760	14.9%	4,049	4,711	8.0%	461	0.8%	3,678	12,438	21.1%	5,714	58,936
BAHAMAS, THE	147	112	36	18.2%	31	5	2.4%	0	0.1%	0	36	18.2%	48	195
BARBADOS	566	285	282	37.8%	165	116	15.5%	8	1.0%	10	292	39.1%	169	746
BELIZE	122	19	103	75.3%	42	61	44.7%	25	18.1%	8	110	81.0%	7	136
BOLIVIA	4,451	680	3,771	69.1%	1,323	2,448	44.9%	504	9.2%	197	3,968	72.7%	607	5,456
BRAZIL	89,841	65,229	24,612	21.5%	11,413	13,199	11.5%	2,306	2.0%	3,333	27,945	24.4%	9,903	114,592
CHILE	13,760	9,421	4,338	22.1%	3,391	947	4.8%	488	2.5%	1,322	5,660	28.8%	2,202	19,645
COLOMBIA	13,853	5,729	8,124	47.8%	5,612	2,512	14.8%	1,098	6.5%	0	8,124	47.8%	1,609	17,001
COSTA RICA	3,531	1,550	1,980	43.7%	992	988	21.8%	486	10.7%	71	2,051	45.3%	511	4,530
DOMINICAN REPUBLIC	3,216	843	2,373	60.5%	744	1,629	41.5%	742	18.9%	218	2,591	66.0%	372	3,923
ECUADOR	9,353	5,722	3,631	33.4%	1,933	1,698	15.6%	212	2.0%	405	4,036	37.2%	1,082	10,864
EL SALVADOR	1,630	69	1,561	86.4%	777	784	43.4%	709	39.3%	11	1,572	87.0%	110	1,806
GRENADA	65	2	63	84.2%	33	30	40.1%	0	0.0%	1	64	85.6%	9	75
GUATEMALA	2,131	458	1,672	63.5%	892	781	29.7%	282	10.7%	88	1,760	66.8%	301	2,633
GUYANA	905	214	690	41.9%	350	340	20.6%	87	5.3%	110	800	48.6%	633	1,647
HAITI	683	66	617	75.0%	429	189	23.0%	134	16.3%	47	664	80.7%	92	823
HONDURAS	2,739	479	2,260	68.1%	1,347	913	27.5%	441	13.3%	37	2,297	69.2%	444	3,318
JAMAICA	3,512	565	2,947	68.5%	1,094	1,854	43.1%	813	18.9%	483	3,430	79.7%	267	4,304
MEXICO	81,207	65,185	16,022	15.8%	10,333	5,690	5.6%	1,692	1.7%	4,804	20,826	20.5%	8,097	101,566
NICARAGUA	6,744	1,334	5,410	67.2%	921	4,489	55.8%	252	3.1%	0	5,410	67.2%	1,308	8,052
PANAMA	3,625	2,237	1,387	24.7%	1,005	382	6.8%	207	3.7%	328	1,715	30.5%	1,667	5,620
PARAGUAY	2,091	821	1,270	50.9%	778	493	19.8%	38	1.5%	0	1,270	50.9%	375	2,493
PERU	12,475	6,219	6,256	33.7%	2,030	4,226	22.7%	718	3.9%	801	7,057	38.0%	3,880	18,579
ST. VINCENT	42	0	42	92.7%	34	8	18.6%	1	2.0%	0	42	92.7%	3	45
TRINIDAD AND TOBAGO	1,717	1,358	359	18.0%	67	292	14.6%	108	5.4%	114	473	23.7%	163	1,994
URUGUAY	2,953	2,294	659	17.2%	565	94	2.5%	54	1.4%	309	968	25.3%	477	3,825
VENEZUELA	25,413	24,962	451	1.3%	246	205	0.6%	43	0.1%	0	451	1.3%	4,361	34,657

Sources: The global debt figures comes from the 1989/90 World Debt Tables of the World Bank.
The USG figures come from the Status of Active Foreign Credits as of September 30, 1989 and shows the outstanding disbursed principal; interest more than 90 days overdue was not added in.

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Mr. ARONSON. If you want, I will just very, very briefly touch on some of the major debtors in the terms that you ask. If you take the largest debtors, I think Brazil, Argentina, Mexico, Venezuela, clearly the most progress has been made by Mexico.

I would emphasize one point, because you said it yourself: there is no magic solution to the debt crisis that does not begin with each country's political and economic leadership making a fundamental decision to create a viable economic structure and to open up to external investment and to reduce protectionist barriers. We cannot make these economies viable if there is not a will to make them viable internally. That is the bad news.

But the good news is that there is an intellectual revolution in this hemisphere in economic policy. President Salinas is maybe the most visible model who has essentially revolutionized his country's economy, is in the process of doing so in very rapid order, and the results are already visible.

As I said in my opening statement—I think you had not arrived then—the conventional wisdom about Mexico a year ago was that it was on the border of economic and social crisis, and people were debating whether Salinas would survive. The Mexican economy grew approximately 2.9 percent last year. After the debt agreement with the banks was reached, domestic interest rates fell 23 points.

That reduces their internal debt, simply because it is driven by interest rates, about $10 billion. It has gone up a little bit, but that was a major savings. You have had capital flows starting to come back in.

So those countries that have started on this process of serious economic restructuring have seen real benefits, and they have allowed us to then work with them and the banks, so it is primarily a private negotiation, to reach successful debt agreements.

Venezuela just announced yesterday a similar, though slightly different configuration, of a debt agreement that will similarly reduce the net debt servicing for Venezuela over the next several years. But again, that was successful because President Carlos Andres Perez and the Venezuelan Assembly stayed the course on a tough economic reform program, which was not politically easy for them to do.

Argentina is a mixed story. President Menem took office, as you know, under extraordinary circumstances. The country was in such deep economic crisis due to hyperinflation that the inauguration was moved ahead by several months. He announced a very far-reaching and revolutionary economic program for Argentina, which essentially was aimed at reversing the history of 50 years of accumulation of state power over the economy.

It has been partially successful, but it still has some way to go. We were in Argentina last week and met with President Menem. He is fully committed to seeing that policy through. He has to take some additional steps on the fiscal deficit side in order to come into compliance with the IMF. Once that happens and if that happens, we would then be in a position to try to move forward under the Brady Plan, and we are hoping that he is successful. We have great confidence in President Menem, but he faces a tough, tough challenge.

Brazil, which is the largest debtor nation—I think it is about $112 billion now—again you have a brand new President who just took office a week ago, and in his first day in office laid on the table of the Assembly again a revolutionary and far-reaching economic reform program.

Brazil has certain inherent strengths that Argentina did not have. It still has a favorable trade balance, it has a very strong productive economy despite an awful lot of excess control and subsidies and the like. We are optimistic about Brazil, but it is a tough road that President Collor has set out on.

In Central America, the most successful debt strategy has been pursued by Costa Rica, and again because they set in place successful economic reform programs.

OPENING TRADE WITH LATIN AMERICAN COUNTRIES

There is another side to this story and I would like to just end with this point. We are asking these countries to open up their economies, to go from essentially a closed, statist, inward-looking model to an outward-looking trading model open to competition.

It is incumbent on us when we are preaching this gospel that we practice it ourselves, and frankly we do not always do so. The CBI legislation is before the Congress now. We have asked for some very modest enhancements that would allow non-leather footwear and some textiles to come into this country duty-free from the Caribbean and Central American countries.

It will help Panama, it will help the Dominican Republic, it will help Nicaragua when it becomes eligible. And it got shot down in the Senate Finance Committee because somebody made the old argument that it is going to cost jobs in this country.

The truth is that, the way the legislation is configured, it will ultimately protect jobs. But we need to get serious ourselves. If we are going to urge all these countries to open up and be free traders, we need to do a better job ourselves to support them when they do.

Mr. COLEMAN. Thank you, Mr. Chairman.

Mr. OBEY. Mr. Lewis.

REWARDING NEW DEMOCRACIES

Mr. LEWIS. Thank you, Mr. Chairman.

Mr. Chairman, let me mention that in the last several months we in the House have experienced a rather incredible level of euphoria relative to that which is happening in Eastern Europe. We have had two great speeches from new leaders in the region encouraging us about the flame of democracy in Eastern Europe. We have seen the potential of elections there, and we have expressed a great deal of support and confidence.

We have also, in expressing that support, given strong indication of our faith in and praise for the people of those countries. Strangely, we tend to fail to give similar expressions, verbally and otherwise, it seems to me, to people in Latin America who are going through very difficult times themselves and facing challenges that indeed go beyond just being life-threatening.

That which has happened in Panama and Nicaragua and Guatemala, indeed El Salvador, is very, very important in terms of our hopes for freedom in our own hemisphere, and I wonder if indeed we are not overdue in focusing our attention on the courage of those people and establishing lines of communication that reflect our interest in their continued and increased success.

Mr. Secretary, I would specifically mention to you that no small amount of praise and credit is due the Administration for their efforts on behalf of a bipartisan and I think significant contribution to the success that has taken place in Panama and Nicaragua especially. I would suggest that maybe, if we accomplish nothing else in the year ahead of us insofar as Central America is concerned, that there is a challenge before us to come to this committee, to the Foreign Affairs Committee, to deal with our chairman and others relative to a similar effort insofar as El Salvador is concerned.

There is not any political credit in our districts one way or another. Our folks want us to get out of Central America in terms of contributions: Why are we wasting money in rat holes around the world?

Indeed, I really do think it is possible that the Administration could play a key role in helping us accomplish a bipartisan success there as well. It would pay a lot of dividends and I would hope that you would really focus upon our committee, our chairman, and others of course in that connection.

I could not help but be struck by your saying that democracy is the watchword in Central America and they are looking with wonder as to whether the United States is willing to take yes for an answer. I certainly hope that we are willing to take yes for an answer, and I hope that our appropriations reflect that as we go forward in this process here.

U.S. TRADE POLICY WITH LATIN AMERICA

Ending these comments with a question that relates to your last statement—all of you could comment any way you would like, but yesterday morning I was in a relatively private session with our ambassador for trade, and I asked a question about Latin America and I did not get very much of a response in terms of real policy direction shift insofar as our attitudes about American restrictions upon trade with our Latin neighbors.

Is the State Department or are other agencies dealing with foreign affairs actively involved in attempting to see existing programs and agreements better implemented, expanding opportunities for open trade, overcoming the resistance to some of that trade that exists here in the United States? What is happening and where can we help?

Mr. Aronson. Congressman, that is a good question, because increasingly if you go to Latin America, as you do, or the Caribbean, what these leaders are asking for is not direct aid in many instances. It is expanded trade and access to U.S. markets and liberalized terms.

We have to make a decision as a country: are we going to have a broad vision of our interests in this hemisphere and take on some domestic special interest or are we going to simply always succumb to the lowest common denominator?

In terms of what we are trying to do, I think we are pursuing trade liberalization in two different, three different ways. One is legislatively, as I mentioned, the CBI. That is going to be back up before the House, and you would make the leaders of many small and needy and deserving Caribbean and Central America countries very happy if we added on those small enhancements that the Administration is seeking. That is one vehicle.

The second vehicle is through the Uruguay Round of the GATT, and there we are seeking, as you know, on a worldwide basis to reduce subsidies for agricultural products, which if we succeed will not only be good for us but will also be good for agricultural producers in Latin America, who pay the same price as we do for subsidies that are largely from the Europeans and the Australians and others.

We are also seeking to rationalize the sugar program, which again has deeply penalized the small sugar-producing countries, and we would like to solve it legislatively, but under the GATT we have to do it multilaterally. That is another area in which we are trying to do it which will have a direct benefit for Latin America.

Finally, the President has been very clear in his message to the State Department and his Special Trade Representative that he wanted us to look for special ways to be supportive of these countries, and particularly the Andean countries. When he came back from Cartagena, he heard a loud message and a strong plea from these three Presidents, who were saying to us: We are willing to accept your strategy; we are going to devote more military and police and security assets to breaking up the drug cartels. But if we are successful, we are going to put a crimp in a certain illegal flow of foreign exchange into our country. We do not want to be dependent on that and we are not, but we want to develop alternatives, and that means trade help.

The President has already put into effect some initial trade liberalization with regard to the Andean countries. We are currently looking at a new package which we hope to present to him for a decision. But this is an area where I think we all have to look anew and to be much more aggressive and thoughtful and creative.

Again, I would like to make a point. I understand the politics of foreign aid always sounds negative, but one of the messages we have to bring to the American people is that the growth of this hemisphere means jobs for Americans, it means increased revenues for state, local, and Federal government. Every billion dollars in U.S. exports going to Latin America is 25,000 jobs in this country.

Last year we exported $43 billion to this hemisphere, and the countries that are reforming economically are the ones that we are exporting more to. Chile, our exports went up 34 percent last year; Colombia, 25 percent; Venezuela, 28 percent. Mexico, two-way trade, as I said, has increased 40 percent in the last two years.

So we have a big stake in this and we need to think creatively.

Mr. OBEY. Thank you.

Mr. Wilson.

BUDGET REQUEST—COSTA RICA

Mr. **Wilson**. Thank you, Mr. Chairman. Would general questions, Mr. Chairman, on the budget be in order?

Mr. **Obey**. Sure, it is your time.

Mr. **Wilson**. Okay. Mr. Secretary, again I want to underline what everybody else has said about what stupendous things are happening in Central America and elsewhere in the world. Certainly, certainly that is a very bright spot.

In a general, very general way, are your requests this year overall any less for any of the Central American countries than we provided last year?

Mr. **Aronson**. I think our request for ESF for Costa Rica this year is $40 million, and I believe last year we may have asked for $57 million.

Mr. **Wilson**. I believe the subcommittee raised Costa Rica last year.

Mr. **Aronson**. You did, correct.

Mr. **Wilson**. What did you ask for last year?

Mr. **Aronson**. I think we asked for $57 million. You raised it to $90 million and then, because of the Gramm-Rudman squeeze and the earmarking squeeze, they wound up getting $63.5 million.

Mr. **Wilson**. And you are asking for how much?

Mr. **Aronson**. We are asking for $40 million for '91 in ESF. I would note, however, that we played, I think——

Mr. **Obey**. Excuse me, could I interrupt. I was talking to my staff. Did you suggest that we earmarked money for Costa Rica?

Mr. **Aronson**. No, no, I did not suggest that, Congressman.

Mr. **Wilson**. I remember that we raised Costa Rica last year, so I was trying to get an idea of what they are asking for this year in comparison with what they actually got last year.

Mr. **Obey**. Okay, because the committee did not raise Costa Rica.

Mr. **Wilson**. I thought we did.

Mr. **Obey**. We did not earmark. We simply tried to prevent Costa Rica from being singled out for reductions vis-a-vis other countries, but we did not, to the best of my recollection, earmark anything for Costa Rica.

Mr. **Aronson**. No, no. Congressman, there was earmark of proportionality put in among the four. The point I was making was that, while the final appropriation was $90 million for Costa Rica, they wound up getting $65 million, because under the pressure of Gramm-Rudman and earmarking generally we had to cut the countries that were not earmarked and Costa Rica, as well as all the other Central Americans, were cut. That was the point I was making.

Mr. **Wilson**. I would generally think the committee has traditionally protected Costa Rica, and I do not know what the budget pressures are going to cause, but I would hate to see them reduced.

Mr. **Aronson**. Well, Congressman, I understand that and, you know, if you want to point to a country that does it right, this is the country. I mean, it is peaceful, it is humane and decent, democratic. They have a police force, not a military. They live in peace with their neighbors and, more than any other Central American country, they try to respond to the needs of poor people.

The problem you have is you have a limited amount of money and where do you give it? The reason we are reducing Costa Rica is not that to be punitive, but for two reasons: one, because the debt negotiation will provide them a different form of economic help, but substantial, that will relieve a substantial burden of debt service, which is an equivalent to direct aid which they did not have before; and secondly, because their economic performance is so good that, compared to some of the other countries in need, they need it less.

Now, I know my friends—if the Ambassador from Costa Rica is here, he will not like me to say that. But those are the reasons. There is no desire to single them out, and I know in the past there was a fear that for political reasons they were being singled out. I can assure you that that is not the case.

It is a question of so many dollars and you have got to give it to those countries that are most in need, and that is where the allocation comes from.

Mr. WILSON. It would seem to me it could be a cause of some political problem, since they have a new administration there. Does it look as though we are disapproving of the new administration?

Mr. ARONSON. Well, I just had lunch with the President-elect of Costa Rica yesterday and I think he knows that he has the strong friendship and support of this Administration. I do not think there is any question about that. And I think he understands the kind of budget constraints that we are laboring under.

Nothing should be read into this except that we have got a tight budget and we have to divide up the dollars as best we can.

Mr. WILSON. Mr. Chairman, would you mind telling me how you feel about that, if you have any feelings about it?

Mr. OBEY. About what?

Mr. WILSON. About providing considerably less for Costa Rica this year than we did last year.

Mr. OBEY. Well, I do not object to the Administration having to reduce funding, because they have less funding available. I simply did not want to see Costa Rica singled out in the region so that they would be the only country which suffered a reduction in aid.

As long as the region is approached consistently, I do not think you can argue with the overall allocation.

Mr. WILSON. Well, we are not reducing aid to Nicaragua and Panama, of course. But are we reducing for Honduras, Guatemala?

Mr. OBEY. Pardon?

Mr. WILSON. Are we reducing for Honduras and Guatemala?

Mr. OBEY. You mean in this year's Administration request?

Mr. ARONSON. We are reducing Guatemala by an equivalent proportion, yes, ESF.

Mr. WILSON. Okay.

Mr. ARONSON. Honduras, I think not.

Mr. OBEY. Were you talking about what the Administration did in their allocations or what they are doing in the budget this year?

Mr. WILSON. I was talking about both. But essentially, I am sort of protesting the idea of providing less money to Costa Rica than we did last year in the final, when the day is done.

Mr. OBEY. In the allocation?

Mr. WILSON. Yes.

I do not have any more questions, Mr. Chairman. I was just curious about that fact. I would like to get your response—you have probably already done this, Mr. Chairman, but did you read about the Senate initiative yesterday to reduce the supplemental by half to Nicaragua and Panama and provide that money to Eastern Europe?

Mr. ARONSON. I read about it, yes.

Mr. WILSON. Do you have any response to that?

Mr. ARONSON. I think that would be about the most tragic mistake we could make toward this region, to do that. As I said earlier, let us not do anything than to set these governments up for an enormous fall, to raise expectations that the United States is going to be serious and for once do it right and then not come through.

I must say, I have listened to speeches about Central America for ten years now, and the people who are proposing that we cut it in half are the ones who have been saying for ten years that what this region needs is not bullets and not military aid, they need economic assistance so poor people can grow and we can have social justice; and that is the root of the problems of the region.

Well, now for the first time in its history, because you have ended these conflicts and you have democracy and stability, you have real economic development and poor people can really benefit. And to hear the people making those speeches saying let us cut it in half perplexes me, to put it in a kind way, and I think that that would be a terrible mistake.

If that is all we can do as a great power, maybe we should just put a sign up that we are not a serious nation any more. 23 Americans gave their lives for democracy in Panama. We have a deep stake in what happens there, and it is not just altruism. That government is led by good, committed people. They have the support of their citizens. But if they do not deliver, if what democracy brings is a declining economy and joblessness and social unrest, who do you think is going to be turned to to maintain stability?

We still have an obligation under the Panama Canal Treaty for ten years to operate the Canal. We have an obligation ultimately, under reservation by the Senate, to ensure the neutrality of the Canal and safe passage. And we have SOUTHCOM there. So we are going to pay now or we will pay later, and I think if we were wise we would do this with economic assistance in a serious way.

Mr. WILSON. Well, I am happy to see you somewhat exercised on the point.

Mr. ARONSON. Strong message to follow.

Mr. WILSON. I am also happy to say that my judgment is that there is a consensus on the committee here that agrees with you. I do not know how serious they are in the Senate about that effort.

Mr. ARONSON. I think it certainly is not driven by the merits or the needs. Maybe somebody thinks that that is a good political gesture, more people from Eastern Europe watching the debate than there are Central Americans.

Mr. OBEY. Let me simply point out, however, that we had three witnesses from the Administration yesterday before this committee. Two out of the three indicated that in their areas, given the changes in Eastern Europe which occurred since we passed the appropriation last year, there most certainly was a demand for some additional assistance.

They did not quantify it, but certainly indicated there was a legitimate substantive need in Eastern Europe for additional amounts beyond those that were provided last year. This was especially true, I will point out, with regard to the Export-Import Bank, where the Senate had imposed a limitation, ill-advisedly in my view, on mid-range credit availability.

I certainly am not endorsing what the Senate did, but I do think we have to understand there is a case that can be made for a modest range of additional assistance in areas like that.

EASTERN CARIBBEAN AND FY 90 SUPPLEMENTAL

I also point out that Secretary Baker, when he testified before us, suggested that the major problem presented to the Administration last year was their inability to respond to Jamaica by providing more assistance, in light of that government's announced intentions to deal with the drug problem.

I hardly think that we would be attacked if we responded to Secretary Baker's observations about that, would we?

Mr. **Aronson**. Congressman, we just secured an additional $10 million in P.L. 480, which will be monetized, for Jamaica in order to make up that shortfall in ESF.

Mr. **Obey**. How much was the shortfall?

Mr. **Aronson**. $20 million.

Mr. **Obey**. It was $20 million, not $10 million.

Mr. **Aronson**. This is true, and we are looking for other ways to make up the rest. But I have the responsibility for all of these countries and I do not want to rob any of them to help another.

But the package of money for Panama and Nicaragua was not gold-plated. Maybe we should have added an extra $100 million of fat for each in the belief that something would be taken out, but we did not. Those are minimal needs. Noriega wrote $940 million in bad checks on the central bank in the last year and a half of his regime, which this Administration is going to have to pay for, the Endara Administration.

We are asking for $500 million.

Mr. **Obey**. Well, let me simply say, when I was at the White House we were not told by Mr. Darman and Mr. Sununu that every last dollar with respect to Panama was inviolate. We were asked whether we could hold reductions to a reasonable minimum, which are the words that I heard in that room.

That is what this committee is going to try to provide.

Mr. **Aronson**. The Administration's view is that the $500 million and the $300 million, with the one agreement that was made on Africa, is really necessary and we hope there will be no reductions.

Mr. **Obey**. Well, I will simply point out, with respect to one additional item—I refer to the A.I.D. item—your word is your bond in this business. When I, on the basis of assurances which I am given by A.I.D., tell a member of this subcommittee that he need not take an action because A.I.D. is intending to take it, then after we support the Administration's position we discover that A.I.D. does not, in fact, take that action, I regard that as a major institutional mistake on the part of A.I.D. You can bet that is going to get corrected in the supplemental, regardless of where that money is going to come from, because I do not intend to——

Mr. **Wilson**. What are you talking about, Mr. Chairman?

Mr. **Obey**. I am talking about the refusal of A.I.D. to provide the assistance that we were told that they were going to provide in the wake of hurricane damage in Jamaica.

Mr. **Aronson**. Mr. Chairman, could you give me some more details?

Mr. **Obey**. It was the eastern Caribbean, which Mr. Gray was interested in dealing with. It was discussed in terms of Jamaica, but it applied to the entire eastern Caribbean.

Mr. **Aronson**. Mr. Chairman, maybe your staff could give us more details about that. I would like to look into it, because I am not aware of it, but I would like to look into it if I could.

Mr. **Obey**. Well, I promise you, regardless of what is in that bill, that is going to get corrected. I am not going to get in the position of telling my subcommittee members something that in fact is not true.

Mr. **Aronson**. Mr. Chairman——

Mr. **Obey**. Mr. Porter.

Mr. **Aronson**. I sympathize with your position. That is the position that we are in and it is not the fault of lack of good faith of this committee and I do not believe, ultimately, the Administration. I do not know the circumstances. We are in the same position, unfortunately, with these leaders.

We say to Michael Manley: Carry out tough economic policies and we are going to provide $25 million. And then at the end of the day we do not deliver.

Mr. **Obey**. All I can say is that the Administration determined that giving money to Tunisia was more important than keeping a commitment which they had made both to the eastern Caribbean and to this committee. So they found a way to provide additional money above original intentions for a non-earmarked country. They asked us to take the earmark out for that country. We did and then they provided the money anyway in that case. I do not regard that as square dealing.

Mr. Porter.

PANAMA DEBT-FOR-NATURE SWAP

Mr. **Porter**. Thank you, Mr. Chairman.

Mr. Schieck, the subcommittee has been looking at a potential debt-for-nature swap in Panama that would be backed by Panama's largest environmental NGO, ANCON, and our own Nature Conservancy. As I understand the swap, A.I.D. would provide $10 million and the NGO's would raise another $5 million, and that would provide a long-term 30-year cash or income stream of $3 million to $5 million to support the watershed of the Panama Canal.

Since we have vital interests in the Canal and this seems to be a careful long-term approach, I support the effort. Do you?

Mr. **Schieck**. Yes, sir. Let me start off by saying I have had the opportunity to have a brief conversation with a representative of the PVO and we have discussed the proposal. I told him that A.I.D. is committed to supporting environmental programs in Panama. In fact we have a program for watershed protection which had been approved just prior to the cutoff of aid during the Noriega time, and we intend to look at it to see if it can be reopened.

We also are interested in a debt-for-nature swap. There are a couple of interesting, not problems, but twists which arise from the fact that Panama operates with U.S. currency. In most countries where we do debt-for-nature, we provide a dollar grant to a PVO, which then buys debt in New York, and then turns it in for local currency to the country.

In the case of Panama, when they turn the debt in, the government must pay out dollars because that is the currency. Since they cannot print the money, they will have to use other resources out of their budget. So of course, the PVO points out that debt that is cancelled will result in a cash flow to the government because they will not have to pay on that debt.

But the fact is that at the moment Panama is not paying on the debt. So in order to do the debt-for-nature swap, Panama is going to have to come up with new resources. It may or it may not be able to do this at this point in time.

We certainly support the idea and will look for ways to implement such a swap and to convince the government of Panama that it is a good idea. But there is this interesting twist because of the local currency situation.

Mr. **Porter**. But the private group in Panama would be a good executing agency?

Mr. **Schieck**. Yes, our understanding of the group is that they are a serious outfit and are on the right track.

Mr. **Porter**. Thank you.

COCA PLANT HERBICIDE TESTS IN PERU

Mr. Levitsky, a few years ago we heard stories about plans to use a pesticide called Spike in a massive spraying campaign against coca leaf producers in the headwaters of the Amazon. I understand there has been a test spraying program. I wonder if you could tell us the results of the test program? Are you finding any lasting effects on the environment?

How do the local residents react to this, and does this give help to the cause of the Shining Path rebels?

Mr. **Levitsky**. We have a cooperative program with the Peruvian government to test Spike and we have a field survey there now. I am not a scientist, but I have seen the results, which is dead coca and green growing under it.

What we are doing now is involved with them, involving ourselves in doing groundwater tests at the site, in other words to see about seepage. As a knowledgeable layman, I would say I think it works and I think it is a big weapon.

Politically, it is not acceptable at this point to the Peruvian government because they point out, and perhaps correctly, that if you wipe out all the coca crops perhaps for 150,000 peasants that are dependent on it, they may be driven into the arms of the Sendero

Luminoso, who exist in the same valley. And there is a linkage, as you know, between the drug traffickers and the Sendero Luminoso.

Our strategy attempts to deal with this in a way that allows the Peruvian government to gain control of the Upper Huallaga Valley through increased military assistance and increased law enforcement assistance and eventually in '91 economic assistance as well, which will in effect lower the price of the coca leaf to the growers—and this has already happened as a result of Colombia, because of the cut in connection between the Colombian traffickers and the growers—and then through law enforcement discourage them from growing it and through economic incentives, and hopefully with a stronger Peruvian economy, begin to attract them off the land.

In that situation, politically Spike could be considered to be the knockout blow. That is, when it becomes effective to use a herbicide that will be environmentally safe, and we believe it is, and knock out large areas of the coca, then we could do it in those circumstances.

So we retain that as a policy. We continue the tests. Last year the Congress gave us about $500,000 to continue agricultural research and we have a contract with the Department of Agriculture on this.

We will have a problem up the way with the manufacturer, who does not want to sell to us because he is concerned about—they are concerned about the effects in the region or protests or something like that. But we will take that on when the time comes.

Mr. PORTER. Thank you very much.

HUMAN RIGHTS SITUATION IN PERU

Mr. Aronson, I have a constituent who tells me she is about to go to Peru to do human rights work. It is my understanding that the human rights situation in that country has deteriorated and the war against the Shining Path guerrillas has not gone very well.

I wonder if you can give me an update on the situation there, and the prospects for change if Mr. Vargas Llosa is elected president?

Mr. ARONSON. I would also just like to offer a suggestion, that your constituent perhaps talk to us before she goes there so we might give her some advice about where to go and where not to go and with whom.

Mr. PORTER. Thank you.

Mr. ARONSON. Because there have been some instances where Sendero has assassinated some U.S. citizens. Just two months ago, they assassinated a young man who was a journalist or was going around trying to do some kind of investigative journalism work. And I just want to make sure she is fully apprised, or he, of the reality there.

I think there has been an increase in some human rights problems and it is brought on by the nature of this insurgency, which is probably the most murderous and militaristic and messianic in the hemisphere. I do not know how much you know about Sendero Luminoso, but these people think that the North Koreans are not committed enough Marxists. They think they sold out because they resumed normal relations with the Garcia government.

One level of the human rights abuse has been their systematic campaign of assassination against villagers who do not agree with their political views, against police, government, military officials.

That having been said, I think also that in the counter-insurgency practices of the army there are oftentimes instances in which the kind of practices that we would like to see are not carried out. And these wars always tend to be very harsh and unconventional, and we are trying to stress particularly now with this Andean strategy, where the military will be more directly involved in the counter-narcotics, that human rights must be a fundamental concern of the military.

In fact, we have carried that message to the president and others and the military leadership, and we have made some particular representations about some instances and individuals that we did not think were carrying out those sorts of practices.

Whether things will change with the new government cannot be predicted. Vargas Llosa is committed to a serious economic reform program, and if there were some relief for the economic crisis that might impact favorably on the insurgency and on the politics of the insurgency, and one might hope. But I think that that is an area where we have to keep vigilant, frankly.

YANOMAMI INDIANS OF BRAZIL

Mr. PORTER. Could I change your focus to Brazil and ask about the Yanomami Indians, who are under great pressure from the military and from miners who have moved in on their tribal homelands. We hear that they are about to be made virtually extinct, at least in Brazil.

What is your reading of that situation?

Mr. ARONSON. Congressman, I would like to get back to you on that because, although I saw some reports a few months ago, I cannot give you a very incisive up to date report.

[The information follows:]

Evidence suggests that, as a direct consequence of the influx of illegal prospectors, the number of Yanomami who died from mercury poisoning or in epidemics of infectious diseases has been increasing.

On January 2, 1990, the Brazilian Government began a program to alleviate the plight of the Yanomami Indians by providing immediate medical treatment of the Indians, removing the approximately 40,000 illegal miners in Yanomami lands, and ensuring that the miners do not return to the Yanomami sites. By February, an estimated 8,000 miners had been moved from Yanomami Indian lands. Federal authorities, however, ran into opposition from the state government of Roraima, whose income relies on mining, and the miner unions' protests that the federal government's actions impeded the work of legitimate miners.

President Collor's first official visit outside the capital of Brasilia after taking office was to the state of Roraima on March 24, 1990, where he reviewed, among other things, the illegal mining problem. After meeting with Yanomami and prospector representatives, he ordered the Federal Police to dynamite clandestine landing strips which serviced illegal mines in the area. Collor indicated he believes that measures which would create more ordered mining in the area are absolutely essential to the rights both of the Indians and of the miners. Collor stated he recognized mining as the economic base of the state of Roraima, but said it must be pursued in a more orderly and environmentally compatible manner.

We are encouraged by President Collor's preliminary measures to halt the illegal mining of Yanomami lands. We expect that he will continue efforts to halt the illegal mining in Yanomami lands and to seek a mutually agreed upon solution between the Yanomami and those legally mining in Roraima state.

Mr. ARONSON. But I would note that President Collor has appointed as his chief environmental policymaker, the equivalent of our head of EPA, an individual who has been noted in Brazil and the world as a leader of the environmental movement. It is a very bold and courageous move. This is the individual who really is a leader in environmental issues in Brazil.

So I think that that is a good sign that this new administration is going to be very sensitive to that issue. But I would like to get you more direct information in a follow-up if I could.

STATUS OF BRAZILIAN ECONOMY

Mr. PORTER. Speaking of radical moves and Mr. Collor, what about the anti-inflation measures that he has instituted? What do you think are the chances of success there? The economy is pretty much going down for the third time.

Mr. ARONSON. Well, the economic picture is really mixed. As I said earlier, there is a lot of productive strength. They still maintain a favorable trade balance and the Brazilian economy grew, I think, by a few percentage points last year.

But they face hyper-inflation, which will destroy any economy and ultimately threatens democracy. The good news about what the new president has done is that he has rightly read the lessons of the past and insisted that it be done quickly and comprehensively. He is not trying to combat hyper-inflation through piecemeal, gradual, incremental measures.

If the congress supports the proposals, we think that they are very, very good and important steps, and we hope that they will be successful and we certainly, along with the IMF, the World Bank, and the IDB, are going to work very closely with the new government and try to be supportive. So far we think he is off to a very impressive start.

We should know in the next six to eight weeks whether initially hyper-inflation has been combatted. But the kind of proposals that he has offered should be pretty effective.

Mr. PORTER. Thank you very much.

Thank you, Mr. Chairman.

EL SALVADOR AID ISSUES

Mr. OBEY. Mr. Aronson, I want to run through a number of questions and I would appreciate very short, concise responses from you.

What year did we start providing aid to El Salvador?

Mr. ARONSON. Well, I do not know the answer to that, but I suspect it was——

Mr. ROWAN. 1980.

Mr. ARONSON. No, it was not, because we had modest aid in '79, I think, because Carter cut it off.

Mr. OBEY. We had the debate on the provision of non-lethal military aid for the first time in what year? Was it not 1980?

Mr. ARONSON. Probably so, yes.

Mr. OBEY. I remember. The day was almost ten years ago today. It was March 24th, and we had an Administration request to renew non-lethal military aid. We were given all the reasons why we ought to do that, all the hopes that we were going to stabilize the economic situation, that we were going to convey to the rebels that they had to negotiate. This was going to give us leverage to deal with the right wing. We were going to be able to push ahead with land reform.

How much have we provided since 1980?

Mr. ARONSON. Oh, I suspect about somewhere around a billion dollars, but I do not have those figures in my head, sir, in military.

Mr. OBEY. No, total aid to Salvador.

Mr. ARONSON. Oh, I am sorry, total aid.

Mr. OBEY. Total aid to Salvador.

Mr. ARONSON. $3.8 billion, economic and military.

Mr. OBEY. Okay. How many Salvadorans have died since that time?

Mr. ARONSON. Well, the numbers that are usually quoted in the press I think are somewhat larger than the actual numbers. They are hard to determine.

Mr. OBEY. Just give me a number.

Mr. ARONSON. But I would estimate somewhere between 40,000, 50,000.

Mr. OBEY. I see numbers approaching 70,000.

Mr. ARONSON. Yes, so have I.

Mr. OBEY. How many Americans have been killed since that time?

Mr. ARONSON. In El Salvador? You are talking about civilians, military personnel? Any American citizen?

Mr. OBEY. Just Americans.

Mr. ROWAN. Seven military, American military.

Mr. OBEY. Are there not 14 in total who have been killed?

Mr. ARONSON. That sounds—you know, I could not tell you the answer to that question, and I do not want to guess. It is too grim a subject.

Mr. OBEY. What is the unemployment rate in El Salvador?

Mr. ARONSON. Probably upwards of 30 to 40 percent, I would think.

Mr. OBEY. How many military officers have been convicted of crimes associated with human rights violations?

Mr. ROWAN. I believe that answer is none, sir.

Mr. OBEY. What is the living standard? How does the living standard today compare for the average Salvadoran versus 1980?

Mr. ARONSON. Do you want to speak to that, Fred?

Mr. SCHIECK. The economic growth is——

Mr. OBEY. I mean, what is the numerical estimate?

Mr. SCHIECK. Okay.

Mr. OBEY. In other words, real income?

Mr. SCHIECK. Per capita GNP now is $860. I imagine that is slightly lower than in 1980, but on an upward trend.

Mr. OBEY. Okay. What percentage of Salvador's budget comes from U.S. sources each year?

Mr. SCHIECK. On the capital budget, which is spending on schools and hospitals and roads, it is probably 95 percent.

Mr. OBEY. I mean, that would not be fair to the Administration's position. It is not that high. What is the overall portion?

Mr. SCHIECK. The overall budget, you mean including operating budget?

Mr. OBEY. Out of the Salvadoran budget each year, how much of that is provided by the U.S.? I mean, the U.S. contribution to Salvador this year represents what portion of the Salvadoran annual budget?

Mr. ARONSON. I do not know the answer to that.

Mr. SCHIECK. No.

Mr. OBEY. Is it above 50 percent?

Mr. ARONSON. I would suspect so.

Mr. SCHIECK. Right, once you throw operating and capital together.

EL SALVADOR HUMAN RIGHTS

Mr. OBEY. Has anybody been tried because of the Archbishop Romero case?

Mr. ARONSON. I think not.

Mr. OBEY. How about the Sheraton murders of Mike Hammer and Mark Perlman? Where are Lieutenant Lopez Sibrian and Captain Eduardo Avilla now?

Mr. ARONSON. In that case, the two trigger men actually were tried and convicted, and then I think they were amnestied in Duarte's amnesty of the FMLN and some political cases. The two former officers that you mentioned are no longer on active duty, I believe. But where they are I do not know. I cannot tell you that.

Mr. OBEY. I would appreciate it if you would supply it for the record.

Mr. ARONSON. Sure.

[The information follows:]

Lopez Sibrian has been in pre-trial detention since 1986. He is accused of involvement in the Kidnapping Ring uncovered that year. We do not know when his case will come to trial. He has been retired from the Armed Forces.

Avila was retired from the Armed Forces in 1986. His present whereabouts are unknown.

Mr. OBEY. What about the Los Hoyos massacre in '83? Where is Colonel Elmer Gonzalez Arojo?

Mr. ARONSON. He is retired.

Mr. OBEY. Has he been charged with bribery in the NORDAC case regarding the sale of defective ammunition involving U.S. funds?

Mr. ARONSON. The charges were dropped.

Mr. OBEY. By whom?

VOICE. The Salvadoran judiciary system.

Mr. OBEY. The good old Salvadoran judiciary, okay.

What about the San Sebastian massacre in '88, ten civilians murdered? Are the major and the lieutenant still in detention?

Mr. ARONSON. Yes. That is a case that is more recent and that we were involved in, and we again brought it to the attention of the government in February. There is a major and a lieutenant who are in custody without pay. There are all awaiting trial, and in fact I think that trial should start relatively soon.

Mr. **Obey**. What is the status of the murderers of the four U.S. Marines in the Zona Rosa case? Are we expecting a trial? If so, when?

Mr. **Rowan**. We are expecting a trial in that case, sir.

Mr. **Obey**. When?

Mr. **Rowan**. Do not know.

Mr. **Obey**. That is all right, you can get it for the record.

Mr. **Aronson**. I have some information on that if you want it, Mr. Chairman.

Mr. **Obey**. Well, why do you not provide it for me.

Mr. **Aronson**. Okay.

[The information follows:

There are four suspects in pre-trial detention in connection with this crime. The defendants' lawyers have filed writs of *habeas corpus*, arguing that the defendants should have been released under presidential amnesty for political offenses mandated by the Esquipulas Accords of 1987. The Supreme Court has not ruled on these writs. We cannot predict with any certainty when this case might come to trial.

EL SALVADOR MILITARY ABUSES

Mr. **Obey**. I want to read from an article in the New York Times a couple of statements describing the Salvadoran military: "An officer taking command of one of the three regional brigades had at his disposal a vast system of patronage and draft, with countless opportunities for enrichment. Colonels leased troops as guards or laborers to local businessmen or even in some cases as hired killers to ensure labor peace, and there was always more money to be siphoned off from the bases' payroll and food budgets."

Then it goes on to say: "Since the Salvadoran Army has no central roster, every year the 14 commanders divide 20,000 pay slots among them, to be assigned at the commanders' discretion. 'Just about every brigade lists at least one 50-man company that is not there,' said one major. Each of these 50 slots pay colones, equivalent to about $100 each month. Times 12, that is $60,000."

Is that an inaccurate statement of the structure of the Salvadoran military?

Mr. **Aronson**. I read that Times article when it came out, which was a few months ago. As I remember, and correct me if I am wrong, the first part of the statement you read was referring to the early 1980's, not the current situation.

As far as the duty rosters, I have to get back to you on that. Do you know, Henry?

Mr. **Rowan**. I do not.

Mr. **Obey**. This article was written in '89.

Mr. **Aronson**. I know that. I am saying the first part, where it says that they loan out guards, to be killers and the like, I think that allegation was referring to the early eighties.

Mr. **Obey**. Here is what I am trying to get at. Do we have anywhere in our government an estimate of how much of our aid we think has been ripped off?

Mr. **Aronson**. My understanding is that most of the military aid—and I would ask Secretary Rowan to talk to that—is that it is basically procured under our direction and that it is not cash in any form at all, it is equipment; and that under that system virtually none of it can be ripped off.

Mr. OBEY. I understand. But as the Secretary of State told us when we were discussing the Middle East, money is fungible. So what I am trying to determine? Let me put it this way. Do we have any estimates about how much has been ripped off illegally by elements of the Salvadoran military?

Mr. ARONSON. Of military aid?

Mr. OBEY. If you do not want to describe it as military aid, how much has the Salvadoran military ripped their own government off? We must have some internal estimates of that, do we not?

Mr. ARONSON. Ripped their own government off?

Mr. OBEY. Yes. I mean, through practices. I would call claiming the existence of a 50-man company, receiving reimbursement, and pocketing the compensation for that non-existent company as ripping the government off.

Mr. ARONSON. I would just like to make one distinction, if I could. The reason I made that point about the nature of our military aid is that my best understanding of how our military aid is provided to El Salvador, there is virtually no——

EL SALVADOR LEAKAGES OF U.S. AID

Mr. OBEY. Forget that question. I am trying to measure the ability of our government to affect policy and the ability of the Salvadoran government to control activities in order to determine whether our policy is worth pursuing or not. So my question is, do we have an estimate of how much we think these kind of games cost in terms of dollars? Dollars which are supposed to be going to provide for the defense effort or the attack against the guerrillas, but instead are just going into somebody's pocket so they can buy another Mercedes.

Mr. ROWAN. Mr. Chairman, I do not have such an estimate with me and I do not know for sure that such an estimate has been done. This is something which we take seriously and we did change our practices in 1984 because of concern about corruption. We will do what we can to generate some materials that respond to your question, but we do not have it here.

Mr. OBEY. Let me say, I find it mind-boggling if after ten years of providing aid, we do not have some estimate of how much leakage there was in the system.

Mr. LEWIS. Mr. Chairman, could I just add to that? I think you are onto a very interesting line of discussion, and I think it is appropriate that we begin to ask these questions. I would say that I have had similar questions regarding what I consider to be my second country, India, for a lot of years, and over the last 20 years we have not really effectively asked those questions, nor gotten answers.

Mr. Secretary, if you would, in responding to the chairman's questions about El Salvador, I would appreciate if you would add material that would give us an indication of a similar pattern of questions and answers for the seventies, and would you also do that for Nicaragua for the same period of time.

[The information follows:]

State Response. We provided miniscule amounts of military assistance to El Salvador during the 1970s. In 1977, the Salvadoran military dictatorship refused our assistance rather than accept our conditions that human rights abuses be stopped.

We resumed military assistance to the reform junta in 1980; the assistance was suspended after the killings of the churchwomen in December 1980, then resumed by President Carter in January 1981.

Mr. ARONSON. Okay. I would just like to make a point, though. I do not want to leave the implication that, even though we are not representing the government over the last ten years, that U.S. economic assistance or military assistance has been provided to El Salvador or any other government in this hemisphere in a leaky manner.

I think that we have very tight controls over our money. You are asking a separate question, which is how much corruption there is in this system, and that is a tough question to answer because we do not have internal controls over it. But we will try to answer it.

Mr. OBEY. My point is, my taxpayers are smart enough to understand, even if people inside the Washington Beltway do not. We provide more money per capita to El Salvador than any other country in the world except Israel. If we are asked to increase that number this year, as we are by the Administration, we have got an obligation to know the quality of the information upon which you are making the judgment that our policy can be successful.

I do not want to be in the perpetual motion business of pouring money down a rat hole. I think that is what we are doing. And my point is, if you are asking us for more money, I think you have got an obligation to know what the answers are to these questions. We have got an obligation to know before we provide any money.

Mr. ARONSON. I do not disagree. I was just trying to define the nature of the question, Mr. Chairman, that is all.

Mr. OBEY. All I am suggesting is that we provide $300 million, $400 million, $500 million a year, or whatever the number is going to wind up being, and we are making up more than 50 percent of the Salvadoran budget, then we need to know the magnitude of what is at risk of being leaked away. Whether somebody wants to say it is direct or indirect, the results are the same. We do not get the bang for the buck that people think we are getting, and maybe that is one of the reasons that it has been taking so long for American policy to work. I think we need some measurements.

EL SALVADOR ARMED FORCES SOCIAL SECURITY FUND

Let me go on. The article talks about the army's main cash reserve and social security funds, called the Social Provision Institute for the Armed Forces. It talks about the armed forces opening their new bank, and it says: "If the armed forces do open their new bank, the profits from fishing and duty-free television sets will be pocket change and the balance of power between soldiers and civilians will be permanently altered."

How do you feel about that question?

Mr. ARONSON. Well, I think the truth is that if you look seriously at the balance of power between civilian and military in Salvador over the last ten years, that nobody seriously could question that the balance has not shifted toward civilians.

Mr. OBEY. The key question is whether or not the military has been able or elements within the military have been able to build up independent sources of financing which are so significant that the ability of the civilian government to control them is going to be brought into question?

I am simply asking your judgment on whether that point has been reached, or whether or not we have been able to back away from that point, or where we are on that spectrum?

Mr. Aronson. The principal fund that is described in that article is a disability and retirement fund that the military has set up and that is self-financed from members of the military, and whose proceeds are used to help pay the costs of widows of soldiers who are killed in battle, disabled soldiers, and retired soldiers.

It has grown to pretty large dimensions, in part I think because all the soldiers who run through the system contribute, but most of them are conscripts, so they are there for two years. So they pay their two years towards retirement, but they never retire. So it is a pretty substantial fund.

I have never seen any analysis or cable or suggestion that that fund in and of itself is so large that it deprives the civilian government of fundamental control over the finances and economy of the country.

But there is a lesson in Panama that I think is important and that you are raising, and that is that the military historically in these countries has been an impediment to democratization. The militaries are changing, but that is true in Central America, and therefore you have to be especially vigilant about a military institution that is also gaining control over economic power.

So I think those are important questions, and I would like to go back and look at that particular question and come back to you on it. I do not dismiss it. On the other hand, the existence of a retirement, disability and credit union fund in and of itself does not strike me as a problem.

Mr. Obey. I am not concerned about the existence of the fund. I am concerned about who controls it and the impact of that control. I am told our embassy estimates that the current assets in that fund exceed 100 million bucks.

We are told that substantial investments have been made by the military in real estate, including resort properties and office buildings in Salvador. We have a substantial question about the economic strength of the military operation in that society, with interesting implications for the ability of the civilian government to control.

Mr. Aronson. Perhaps. On the other hand, as you know, any pension fund, which is what this is, has to invest its money. They could put it into——

Mr. Obey. Again, that is not the point. I think you know that.

Mr. Aronson. No, I understand. All I am saying is the facts do not—

Mr. Obey. My point is, I would feel more comfortable if Mr. Cristiani had control of that fund, rather than the military.

Mr. Aronson. I think that is a fair point.

Mr. Obey. My question is, do we have any reason to suspect that the military is going to continue to control that fund, rather than the civilian government?

Mr. Aronson. I will get back to you.

[The information follows:]

There are no plans to transfer control of the IPSFA from the military to the civilian government.

Mr. **Obey**. We do not have any guess on that score?

Mr. **Aronson**. I do not know the structure of the fund. I do not know whether it has a civilian board of directors, whether it has some autonomy.

Mr. **Obey**. My understanding is it has never been under the control of the civilians.

Mr. **Aronson**. Well, I would like to find out before I give you an off the top of the head answer.

Mr. **Obey**. Is it General Larios, the current Minister of Defense?

Mr. **Aronson**. Correct.

Mr. **Obey**. My understanding is he has retained control of that fund.

Mr. **Aronson**. It may be true. It may be you have information that we do not have. But I would like to find out.

Mr. **Rowan**. Mr. Chairman, I can tell you a little bit about the structure of it. The Minister of Defense is the chairman of that board of military members. They have a professional manager of the fund. But it is an organization which is run by the military, and so your questions are certainly quite reasonable ones.

Mr. **Obey**. What I am concerned about is that we have something else that is being masked. In this country we have got the deficit being masked by the social security receipts, but at least the administration of that fund is in the hands of benign bureaucrats.

In the case of Salvador, if they have any ability to use the resources from that fund in any way like some of the managers of our pension funds have had in this country, it gives them an opportunity for immense political as well as economic leverage.

Mr. **Aronson**. That is a good point.

Mr. **Obey**. The question is, with that kind of control, with the military attention being focused on investments in resorts and downtown office buildings, I do not wonder that they have not had more success than they have had in pursuing the war.

That is one of the things I am talking about when I am talking about the need for the Administration to make a fundamental reevaluation of the effectiveness of our policy down there.

EL SALVADOR MILITARY RESISTANCE TO NEGOTIATIONS

General Thurman recently testified that the 60,000-man Salvadoran Army could not defeat the 5,000-man FMLN. Does the Administration agree or disagree with that statement?

Mr. **Rowan**. I can comment on that. I just looked at General Thurman's testimony which I think you are referring to, and I do not think he—what he said as I have here is that—Senator Kennedy asked him: "Do you not think that just by sheer force of might that they could squash the guerrillas of Salvador?"

General Thurman: "I think that they will not be able to do that, because the guerrillas have sanctuaries they are able to retreat into and operate out of, and I think they are ultimately going to have to go to the table and negotiate through that position."

I do not know any serious person who has ever thought anything else than that this was going to have to end up with a negotiated settlement, that these people have enclaves that they can retreat into. They have had external support. Perhaps that will dwindle or go away.

This is not a remarkable statement.

Mr. **Obey**. I do not think it is remarkable. What I do find remarkable is that there is a substantial portion of the Salvadoran military that still disagrees with the statement, and therein lies our problem.

Mr. **Aronson**. What makes you say that, Mr. Chairman, that there is a substantial portion of the military who disagree with that?

Mr. **Obey**. I do not see unanimous military support for Mr. Cristiani's efforts to move to the negotiating table.

Mr. **Aronson**. Well, all I can say is what the record shows. He said at his inaugural address that he would negotiate without preconditions——

Mr. **Obey**. I did not say Mr. Cristiani. I said I did not see his position being unanimously supported by the military leadership.

Mr. **Aronson**. Well, the only point I was going to make is that——

Mr. **Obey**. I am never questioning Mr. Cristiani.

Mr. **Aronson**. No, the point I was going to make, though, is that he went to three rounds of negotiations, that in fact there were military representatives at all of those rounds, and they were prepared to go at the third round. They were prepared to go as well, and the FMLN walked away. And there is no evidence that the military has not supported his current initiatives under the UN Secretary General, and I think we are on the verge of serious negotiations again.

I think there is a hell of a lot of suspicion among a lot of military officers about the intentions of the FMLN and whether they are serious about negotiating, but that is not entirely unwarranted.

Mr. **Obey**. What about Vice Minister of Defense Juan Orlando Zapeta, First Army Brigade Commander Colonel Francisco Elena Fuentes, and Seventh Army Garrison Commander Colonel Stabin? Stabin, as you know, has been a key figure implicated by some in a kidnapping for profit ring which preyed upon wealthy Salvadorans.

The pervasive influence of the Class of '66 in the military, many of whom, as you know, have strenuously resisted moving into negotiations. When I have talked to the military down there they have emphasized the difficulty of bringing their military brethren along in support of negotiations.

So I think to suggest there has not been substantial military resistance to negotiations would be preposterous.

Mr. **Aronson**. The point I was trying to make, Mr. Chairman, was that I think that there is a large amount of suspicion and distrust of the FMLN intentions in the negotiations, and there are probably a lot of military officers who do not believe that it is a real exercise, and therefore they are reluctant to go through it because they believe it gives the guerrillas breathing space and time to regroup and to hit them again, which frankly they just went through in the last round.

In fact, the Final Offensive was being planned while the government and the guerrillas were negotiating. And in fact they killed the daughter of a colonel, an active duty colonel, while the government was sitting down negotiating.

So the military says to themselves, some of them: This is all propaganda and public relations.

Mr. **Obey**. That is a legitimate concern and I frankly share their suspicion with respect to certain elements of the rebels. I will suggest there is another reason why many military people do not want to go into negotiations, not the least of which is that the war itself has enabled the military to expand its size, to provide more career opportunities, to provide more opportunities for personal enrichment and all the rest.

The military runs the telephone company, does it not?

Mr. **Aronson**. There is a military officer who has been appointed the director of the telephone company. I do not know if the military's institution runs the telephone company.

Mr. **Obey**. Well, what is the role of the military in distributing U.S. aid under the Hearts and Minds Campaign?

Mr. **Schieck**. There is no direct role. At times, when CONARA is in the field delivering aid, the military is in the area if it is a disputed area. But the military has no direct role.

Mr. **Obey**. How often do they get involved informally?

Mr. **Schieck**. Well, a lot of the activities that CONARA is carrying out, which is being financed with local currencies supplied by A.I.D., takes place in disputed areas. I mean, that is the whole idea of CONARA, to be able to deliver——

Mr. **Obey**. I understand that.

Mr. **Schieck**. And so the military will be around. But basically, it is trying to secure the area for the operations of CONARA.

EL SALVADOR—NEGOTIATIONS AND PROSPECTS FOR PEACE

Mr. **Obey**. My only point, Mr. Secretary, is that since that March date ten years ago we have heard an awful lot of promises. There have been an awful lot of expectations, and we in many ways, not all but in many ways, we still are pretty much at ground zero.

I will agree that, because of the involvement of the UN and the defeat of the Sandinistas and because of the new statements of the Soviets, that there is a greater opportunity now than there has been for some time to reach the negotiating table. I am not certain how long that can be sustained, given the resistance within Salvadoran society.

I think the question is not whether we are comfortable with all elements of Salvadoran society, but if our policy sufficiently strengthens the elements that we think are responsible or not.

That is why I again come back to my suggestion. When we dealt with the Nicaraguan policy, we were told by a key advisor to Mr. Arias. He said, you know, you Americans are funny people. We leave you alone for five minutes and we cannot find you where we left you.

And he said, you know, what you need to do is to simply go home and eliminate whatever portions of your policy are preventing you from getting together, so that over a sustained period of time, no matter which party controls, you have a broad-based policy that can be supported through a series of administrations.

He said, if you have got a policy which can be sustained only by a narrow number of votes, then that policy is going to change every time you have got a different election, and we are going to have some time keeping up with you people.

I think we did approach, in the end, Nicaraguan policy that way, by getting rid of the Contra equation so we could focus on the other pressures brought to bear at that point. It seems to me that we are at the same crossroads with respect to Salvador.

There is a high degree of dubiousness, and I must say I share it, that Mr. Cristiani will be able in fact to obtain enough running room to negotiate in earnest. That is why we need to have a very clearly understood set of principles which lay out what it is that we expect the rebels to do and what it is we expect the right wing military elements to recognize, in return for whatever activities are undertaken on our part.

That is the element that I think is missing from the Administration's policy. Until we have got it, I just find it very difficult to support continued financing for this operation.

Mr. ARONSON. Can I take a minute to respond?

Mr. OBEY. Yes.

Mr. ARONSON. I think that kind of discussion would be very helpful, as I said in my opening statement, and we are prepared to begin that right away as soon as Secretary Baker comes back.

I think, frankly, there is more that has been thought out than perhaps we have articulated, in part because sometimes to be effective in a situation like this it is better for the U.S. not to be trumpeting its agenda, but to be working quietly behind the scenes and to encourage the Salvadorans under the UN's auspices, and I think we have done that.

But that does not mean we do not have to lay out the principles and come to some consensus, because I agree with that.

The second point I would make is that I think it is a mistake and it is demoralizing to us and to our country to sit here and say, ten years later our policy has simply been a failure in El Salvador. I do not think that that is true, and part of what you do—I mean, the fact is as a country we waited too long to defend democracy in El Salvador. We should have been having this debate in 1972 when Duarte won an election, and unfortunately we did not. But we cannot repeal history.

But the last ten years have not been a failure, even though I share your frustration at where we are and I think, frankly, over the recent past we have probably neglected Salvador a little bit. But the fact is one of the things we did is we ensured that the FMLN did not win. And that may not sound like much of a victory up here, but I guarantee you to the people of that country, who fear and by and large loathe these guerrillas who have made their lives hellish, that is a real accomplishment.

Mr. OBEY. I agree with Ambassador White's statement that the worst thing that could happen would be for either the rebels or the government to win an unconditional victory, because in either case, in my judgment, you would then have a slaughter.

Mr. ARONSON. But our policy prevented either of those from happening.

Mr. **Obey**. With all due respect, it may have prevented either of those from happening, but at a cost of somewhere between 50,000 and 70,000 dead.

Mr. **Aronson**. Well, that is the price we pay for waiting so long.

Mr. **Obey**. No, that is the price somebody else paid.

Mr. **Aronson**. Well, I agree with that. But there were times when we had better options and as a country we were preoccupied and we did not defend democracy before there was a revolution, and we ought to learn that lesson.

Mr. **Obey**. You bet.

Mr. **Aronson**. But the second point is the Salvadoran society is not the same society. There is plenty that is brutal and horrible and terrible in El Salvador, but this is a country that for 100 years was a feudal society and a military dictatorship. And they have had real elections.

We had international observers in the last five Salvadoran elections, just like Nicaragua, and the elections were valid and real poor people determined who their leaders were. And it is a country where 20 percent of the land has been transferred from oligarchs to peasants. And it is a country where our aid reduced the infant mortality rate and has allowed some modest growth to begin.

Now the issue is how do you end this war and how do you bring permanent peace, and that is what you are asking. I think that has to be the agenda. But I do not think we should conclude that our money was simply down a rat hole. Things could have been a lot worse and they would have been if we had just pulled the plug in El Salvador.

EL SALVADOR—WITNESS TO THE JESUIT KILLINGS

Mr. **Obey**. All I am suggesting is, frankly, there are reasons that there is so much renewed suspicion of the Administration. One is that I talked to the woman who witnessed the Jesuit killings. We talked to her over two and a half hours. I was frankly appalled to hear the way in which her testimony was handled and the way the embassy appeared to attempt to discredit her testimony after it was given. It just seemed to me that the embassy was acting in such a defensive fashion that it brought into question whether or not the embassy was trying to sell a policy or get at the truth.

When I hear that woman describe what happened to her, I really wonder why on earth it was handled that way and whether or not the embassy is devoting more of its time to defending the Cristiani government than it is pursuing the truth, wherever it lies.

Mr. **Aronson**. Can I respond to that, Mr. Chairman?

Mr. **Obey**. Sure.

Mr. **Aronson**. I would just like to make an appeal to you, which is before you reach that judgment, which is a very harsh judgment about this embassy, I would like you to have a chance——

Mr. **Obey**. I have not reached a judgment. I raised a question.

Mr. **Aronson**. Okay. Then before you answer the question I would like you to sit down with the people, the other people who were in the room with that woman, and hear their side of the story, because—remember that movie Rashoman many years ago?

Mr. **Obey**. I understand.

Mr. **Aronson**. I have no doubt that this poor, humble woman believes everything she told you at the end of the process. But I talked to everybody who was involved, not just one person, and I am convinced that what went on was nothing like the description or the report that was done, which was also based simply on listening to her testimony.

Mr. **Obey**. I am making no judgment about the validity of her testimony. What I am asking is how on God's earth it could have been handled in a way which left people open to so much doubt and confusion?

Mr. **Aronson**. I will tell you the reason: because there was enormous concern in the human rights community that we would not pursue this investigation and that the Cristiani government would not target the military. And this woman appeared and she suddenly was believed to be the key to cracking this case. She said that she saw some military officers.

And the next thing they heard from people who had talked to her was that her story did not turn out. Before checking and finding out the facts, the conclusion was that this was a cover-up.

If you think about it, even if you think that our embassy people are capable of doing that, why would they want to? We want to keep aid flowing to El Salvador. The Congress had just passed a resolution 430 to one or 420 to one saying that the resolution of the Jesuit case would determine whether aid continues to flow. We supported the resolution. The Senate passed the same thing.

In fact, when this witness appeared we were very encouraged. I personally helped get her out of the country and arranged security for her. We were encouraged because we thought somebody was available who in fact could help crack the case.

And she was not mistreated. The problem is that she told a story and her husband told a story, and then she told it again and the elements did not add up. And then as it was pursued it turned out that there were contradictions. That did not make the embassy happy. It demoralized them because they thought that she would help crack the case.

In the end the military was targeted and they were implicated and they have been accused, and the accusation or the belief we were trying to cover it up was not founded. I guess I would just say, let me bring the people who were in the room with her, who sat there the whole time, and I would like you to listen to them and then reach a conclusion.

DRUG INTERDICTION PROGRAMS

Mr. **Obey**. Let me simply say, we have got a vote on the floor and I am going to have to shut this down. But with respect to the drug interdiction and eradication programs, I appreciate your efforts and I appreciate your concerns. I have to tell you I do not think these programs are going anywhere.

Mr. **Levitsky**. Which programs are you talking about, Mr. Chairman?

Mr. **Obey**. All of them. What I am suggesting is simply that we have provided every dollar we have been asked to provide for these programs by the Administration and then some. I really do not think that we have a handle on the situation.

Yes, we have gone after some drug kingpins. Yes, that is fine. I would love to see them all blown away. Yes, we have had some good news about that. But the fact remains, if you take a look at the percentage of the crop that we have been able to wipe out, if you take a look at the percentage of drugs we have been able to intercept before they come into this country, and if you discuss the private concerns of people who have been in this program for the past four years and have talked to us about it, you have to come to a conclusion that they simply are not working very well.

I have a great question as to whether or not the money which is being expended is an effective use of anti-drug money.

Mr. LEVITSKY. Well, I do not know the basis on which you come to those conclusions, Mr. Chairman. But I respectfully submit that you are wrong on the effect of our programs.

We have been spending around $100 million to build the capabilities of other countries. We have built capabilities. We do not do these programs for the other countries. We try to promote and enhance their political will to go after the crops.

You cannot measure success on the basis of the crop itself. What we are trying to do now with the new strategy——

Mr. OBEY. But that is the bottom line result. Building the capability is fine, but what counts in the end is what happens to the crop and what happens to the usage.

Mr. LEVITSKY. That is right, and what happens to the usage is largely dependent on what happens to demand for that crop in the United States.

Mr. OBEY. I understand.

Mr. LEVITSKY. And we have to work on both issues. However, the strategy that is laid out in our cocaine strategy, in the President's strategy, is to work against the entire chain. It is not to eradicate the crop at the farm gate, which would be in some cases counterproductive. It is to try to break the link and to try to harass the traffickers and to try to get at the overall problem in a way that will be sustained over a period of time.

And it is to try to get those growers off the land by strong law enforcement, by lowering the price of coca at the farm gate, which has happened, as you know. It is almost below the cost of production as a result of what has happened in Colombia and Bolivia and to a lesser extent, but to a degree, in Peru.

The strategy is beginning to work, and I would say that that, combined with our strong programs in this country and other international programs to go after money-laundering and chemical precursors, is something that this country has never had before, which is a comprehensive strategy, not something focused merely on destroying the crop with a bunch of weed-whackers, which in fact we used to do and we do not do any more.

Mr. OBEY. Well, I will be interested in taking a look at how much progress we have had a year from now.

CIRCUIT-RIDING RURAL WATER PROGRAM IN EL SALVADOR

I really do not have time left because I have got to make a vote. Let me simply ask, with respect to A.I.D., I understand that the circuit-riding rural water development program that was being pushed in El Salvador has been turned down by A.I.D. I had some concerns expressed by some local constituents involved in that program. I know Mr. Edwards has also.

I would like to have an explanation of why that program was not accepted by A.I.D.

Mr. SCHIECK. Okay.

[The information follows:]

In 1989, officials from the International Rural Water Association (IRWA—the overseas extension of the NRWA) visited El Salvador and Guatemala to discuss project possibilities with A.I.D. Missions in those countries. Subsequently, IRWA submitted proposals to each of the Missions.

The Missions have found IRWA to be a highly professional organization and discussions have been cordial. The primary reason that A.I.D. has not yet been able to enter into an agreement with the IRWA is that the IRWA approach involves larger water systems than those emphasized under Mission country program strategies.

The El Salvador Mission, after preliminary discussions with IRWA, unfortunately was unable to finance IRWA's proposed $500,000 pilot project due to the following:

It had an extremely high per-capita cost as compared with A.I.D.'s new Public Services Improvement project which, along with other infrastructure activities, will support the introduction of rural potable water systems in some 2,000 rural communities.

The IRWA-proposed project seemed more applicable to secondary and tertiary cities of developing countries, where a larger population would be served and the local institutions assisted. Typically, a municipality would have greater management and financial capabilities. Unfortunately, the only municipalities in El Salvador that would meet those prerequisites are involved in an ongoing project with the Inter-American Development Bank to improve the management of the water systems.

When the A.I.D. Mission informed IRWA of its inability to fund the proposed project on February 14, 1990, the Mission recommended an alternative. A.I.D. will be entering into a major technical assistance contract under the $75 million Public Services Improvement project. The Mission suggested that the organization might want to enter into a joint bid on the contract with another consulting firm and indicated that a list of firms would be available from the Mission's contract office soon after the letter was sent. The Mission suggested the joint-bid approach because the contract crosscuts the project components, requiring expertise in both water supply and road repair/maintenance. IRWA's water-supply expertise would need to be complemented by a firm with road repair/maintenance expertise.

Similar to the El Salvador case, the A.I.D. Mission in Guatemala is focusing on community water systems that are smaller than those the IRWA has mentioned in its discussions with the Mission.

IRWA plans to submit a formal proposal to the A.I.D. Mission in April. The Mission will review the proposal and provide a response.

Mr. OBEY. Thank you all very much.

[Questions and answers for the record follow:]

Questions for the Record From Mr. Obey

SUBMITTED TO DEPARTMENT OF STATE

COCA PRODUCING COUNTRIES:

ECONOMIC VS. MILITARY ASSISTANCE

Question. The Administration has targeted military assistance funds for the three coca producing countries in Latin America. First, about $124 million in assistance provided in the FY 1990 bill has been programmed by the administration in military assistance for Peru, Bolivia and Colombia. This is 70% of the funding allocated for these countries in 1990.

In the Administration's request $137 million or 67% of the request has been provided for military assistance.

Why has the Administration targeted military instead of economic or development funding for these countries?

Answer. The administration determined that engaging the Andean militaries in anti-narcotics operations was an important part of the U.S. narcotics strategy to reduce the supply of cocaine coming to the U.S. Significant alternative development funding in FY 91 and beyond, based on counter-narcotics performance by the governments concerned, will anchor the gains made in military and law enforcement actions directed against trafficking interests.

Question. To what extent are the military in these countries fully cooperating on the war on drugs?

Answer. The Colombian military has been fully and successfully engaged in counter-narcotics operations since at least early 1988. Small numbers of the Bolivian Air Force and Navy supply pilots and river units to support police anit-narcotics operations. The highest levels of the Peruvian military have committed themselves to implementing an active counter-narcotics role, once U.S. military assistance begins to supply their units with the necessary resources.

Question. What safeguards are there that military equipment and other military assistance is not put in the hands of military personnel assisting the drug traffickers?

Answer. Military equipment and resources supplied by the U.S. are subject to field end-use monitoring by American personnel and inventory control. These provisions are part of the letters of agreement which are signed between the U.S. and the host country.

Question. In Bolivia the Government refuses to develop a program of forced eradication of coca crops. How will the military funds therefore be used in Bolivia?

Answer. On May 9, the U.S. and Bolivia signed agreements which will provide military assistance to be used in counternarcotics operations. While specific details must be worked out, the army will support police in interdiction of illicit narcotics. Both the Bolivian Navy and Air Force are already engaged in counternarcotics work and have cooperated in seizing the equivalent of 3.5 metric tons of cocaine in 1990. With respect to forced eradication, the Bolivians have reduced over 21,000 square meters of seed beds and conducted forced eradication of mature coca plantings in the Yapacani area virtually eliminating coca there. In addition, during this year alone, approximately 3,000 hectares of coca have been voluntarily eradicated by coca growers, already more than last year's total.

Question. For these countries to develop alternate crops and a non illicit drug producing economy isn't it necessary to provide development type assistance to develop alternatives?

Answer. The Andean Counter-Narcotics Strategy is performance-based. Under the economic assistance component of the strategy, the U.S. will fund traditional alterantive development programs in coca-producing and surrounding areas; project assistance and policy reforms to create alternative sources of jobs, income and foreign exchange throughout the economy; and fast-disbursing balance of payments assistance to finance productive imports and/or service of debt to the U.S. or international financial institutions.

Question. The March 1990 State Department International Narcotics report indicates for Bolivia that "while improved interdiction efforts should result in larger, more costly seizures, noticeable, long-term reductions in cocaine output can best be achieved through a net reduction in the coca crop's size. Since the Government of Bolivia is not willing to force extensive involuntary eradication, reduction means voluntary, manual eradication in the context of a viable crop substitution/alternative development program".

Why doesn't the FY 1991 request for Bolivia reflect an emphasis on economic alternatives.

Answer. We are requesting $86 million in economic and food assistance for Bolivia for FY-91. An additional $65 million in counter-narcotics economic assistance is tentatively earmarked for Bolivia subject to counter-narcotics performance and adherance to sound economic policies.

Question. Last year Congress provided $125 million to be used to help fight the drug war. The Administration was to allocate that funding to countries for economic and military assistance. About $20 million of that funding has been proposed by the Administration to go to the State Department International Narcotics program and about $106 million for military assistance. None has been proposed for development or economic assistance. Why were funds allocated in this manner?

Answer. The President's Andean Counterdrug strategy is designed to be based on counter-narcotics performance. In FY 1990, top priority is being given to strengthening the political commitment and institutional capability of the three Andean governments to deal with the drug problem; increasing the effectiveness of their armed forces and law enforcement activities to interdict the production, processing and transportation of coca within the source countries; and assisting them in disrupting the activities of trafficking organizations in these countries. As efforts to disrupt the drug trafficking organizations break the link between growers and traffickers and to drive down the price of coca leaf at the farmgate level take effect, a significant economic assistance package for alternative development and macro-economic growth is planned for FY 1991. These funds will assist in pulling coca out of these economies and offset the economic costs associated with governmental efforts to combat trafficking.

INCENTIVES

Question. This Committee two years ago initiated a process of incentives for countries making progress on drugs. We set aside both ESF and military assistance for the Administration to provide assistance to countries that demonstrated their willingness to cooperate with the United States on illegal drug control. When the Administration, with urging from the Committee, applied this incentive program there have been some positive results.

However, the Administration has taken the incentive program lightly, and has proposed allocating funds on a "business as usual basis".

For instance, last summer, the Administration proposed allocating $11 million in cash assistance to Bolivia, even though Bolivia hadn't even begun to meet its eradication targets. In fact, a State Department report released a few weeks after the request indicated that Bolivia was actually producing *more* coca, not less.

If we are to provide a total of almost of half billion assistance to Bolivia, Colombia and Peru during fiscal year 1990 and 1991, what incentives for receiving the assistance are you building into the program?

Answer. The military, law enforcement and economic assistance is conditioned upon progress in dismantling narcotics trafficking operations and implementing sound economic policies to stabilize Andean economic structures. U.S. assistance will be allotted according to the degree to which these objectives are met.

Question. Why hasn't the administration used funding to these countries as a leverage for making progress on drugs?

Answer. The narcotics certification process mandated by law links various types of U.S. foreign assistance to anti-narcotics performance. The International Narcotics Control Strategy Report (INCSR) provides the criteria and judgements made by the Administration in withholding foreign assistance to those countries which are deemed uncooperative on narcotics matters. The three Andean countries have had a variable track record in putting "powder on the table" in the past, and the Administration has taken appropriate action, such as the decertification of Bolivia in 1987.

Question. The incentive program allows for funds to be redistributed from countries not making progress on illicit drug control to countries that are making progress. Has this ever been done?

Answer. Since narcotics funding under NSD-18 has not yet been disbursed, a redistribution of resources according to progress has not been done. However, we anticipate that this will be part of the conditions attached to the assistance.

Question. Will the Administration set up an incentive program for funds requested in FY 1991?

Answer. Yes.

INTERNATIONAL NARCOTICS REQUEST

Question. The Administration has requested $150 million for International Narcotics Control programs. This is up from $113 million provided last year and $101 million in 1989—this is a 30% increase.

In January the State Department IG released a scathing report on the operations of the International Narcotics bureau. We'll get into the specifics of that report when we hear from the State IG next week. But for today we need to have your assessment of whether in light of the IG report an increase of 30 percent in funding will have any effect on the reduction of illicit drugs.

Answer. The IG report was misleading in that it reported on certain operations of as long as two years ago. Since then, the IG has acknowledged the great strides made by INM over the past year.

The 30 percent increase in the FY 1991 Congressional Submission is primarily devoted to supporting the Administration's Andean Initiative to enhance our counternarcotics programs in the Region against major trafficking organizations and production facilities of U.S. destined cocaine. We believe that the budget increase supporting this effort and other INM programs will help to reduce illicit drugs entering the U.S. It should also be noted that the increase in reality will only be 13 percent when the $16.5 million in enforcement funding is transferred from the Arms-Export Control Act to the INM account.

Question. One of the largest growing expenses in the program is the interregional aviation support program, which is requested this year at a funding level of $33.5 million—almost 25% of the program. The wing receives more funding than any of the individual country drug control programs.

Is the high cost of this aviation wing taking funds away from individual country programs?

Answer. The aviation wing provides airlift support to the narcotics programs in countries which require this type of assistance. The budget estimates for the airwing are based on projected deployment schedules taking into account past experience and future needs. These costs do not take away funds from country programs and are totally funded in FY 1991 in the interregional aviation support category. In actuality, the aviation wing expenditures really add to the country program level of assistance.

Question. What positive results have you had from the operation of the wing?

Answer. We have helped other governments conduct successful eradication and interdiction operations and wish to expand these efforts in the near future. We are particularly interested in increasing our efforts in the Andean producer nations. The air wing provides support to DEA, other U.S. and host country agencies whose efforts with host government institutions result in the direct seizure of narcotraffickers and illicit drugs and destruction of cocaine laboratories. Without this aviation support, these developing nations often would be unable to accomplish these objectives.

Question. What countries will not allow the operation of the wing within their country?

Answer. No countries have forbidden entry or refused support. Some countries, like Mexico, have their own counter-narcotics air wings and prefer to accomplish this activity on their own. In fact, we have more requests for support than we are able to service on our limited budget.

INTERNATIONAL NARCOTICS CONTROL PROGRAMS:

ROLE OF DEMAND REDUCTION

Question. The President's 1990 National Drug Control Strategy recognizes the critical importance of demand-reduction programs in source and transshipment countries and supports the establishment of drug education and awareness programs overseas. In which foreign countries is the United States currently sponsoring or contributing to demand reduction programs?

Answer. The United States supports demand reduction and public awareness activity in all of the major priority countries: Bahamas, Bolivia, Brazil, Colombia, Ecuador, Jamaica, Mexico, Pakistan, Peru, Thailand, and Venezuela. Additionally, the United States provides a wide range of assistance in demand-reduction and public awareness through regional programs conducted by the U.S. Information Agency, the Agency for International Development, and the Bureau of International Narcotics Matters. Countries in the regional programs include Argentina, Bangladesh, France, the Federal Republic of Germany, India, Italy, Malaysia, Nepal, and Sri Lanka.

Question. Briefly describe one example, say Mexico. What are current U.S. drug-awareness initiatives in Mexico? How might these serve as a model for other countries?

Answer. The three foreign policy agencies—INM, USIA, and AID—collaborate closely in the Mexico program. USIA implements an extensive cultural exchange program with a strong demand-reduction/public-awareness thrust which includes visits between the two countries, VOA programs involving the Mexican press, and interactive media programs between U.S. and Mexican experts. USIA is the primary embassy liaison to the various public and private sector groups. AID coordinates a community-based public-awareness program through an indigenous private, voluntary organization: FEMAP. AID has also produced an anti-drug video with Mexican stars; it will be the basis for a prevention campaign. INM's NAU provides funding to the AID program and has also funded a Mexican epidemiology study. The NAU also supports a sophisticated "training of trainers" program in which a cadre of Mexican professionals is oriented to the use of the INM strategic planning system. They, in turn, will train some one hundred other personnel from the Federal District, where 25% of the national population lives. This training program will be extended to other parts of Mexico.

Question. What percentage of our overall international narcotics control budget is devoted toward promoting drug-awareness and education programs in foreign countries? How do you feel about this figure? Do you feel it should be larger? Are countries requesting more in the way of drug awareness and demand reduction programs than the United States is willing to or capable of supporting?

Answer. Approximately 2.6% of INM's total annual budget is devoted toward promoting demand-reduction/public-awareness. This budget is $113 million of which $2.9 million is budgeted for demand-reduction.

In order for the US to maintain a leadership position in this important area, it is desirable to become increasingly but modestly involved, especially in manpower development, where a relatively small investment provides a substantial payoff in developing host country expertise capable of effectively planning and managing domestic programs.

The US must also be realistic, however, and should not try to shoulder the entire burden. The accelerating calls for assistance would rapidly tax our capability to respond, if we were the exclusive resource. Fortunately, we are not. Increasingly, other developed countries recognize their responsibility. The European Community has provided $5 million for demand-reduction activities in the Hemisphere; UNFDAC has provided grants totalling $1.6 million. Additionally, at least one international bank, the Inter American Development Bank, has also joined our ranks; hopefully, others will follow. Our great challenge now is to coordinate our efforts to make effective use of our scarce resources.

Question. Would you submit to us a country-by-country breakdown of U.S. international narcotics control assistance devoted to drug awareness programs?

Answer. A complete breakdown of U.S. international narcotics control assistance devoted to drug awareness programs would be possible if USIA, AID and INM pooled their information into a single report. We would be happy to prepare such a report for a future date.

INTERNATIONAL NARCOTICS CONTROL: EFFECTIVENESS OF CERTIFICATION PROCESS

Question. U.S. international narcotics-control policy links or conditions U.S. development and military assistance to drug-control efforts of foreign governments. What do you see as the strengths and weaknesses of such a policy?

Answer.

STRENGTHS

The Andean Strategy involves coordinated application of U.S. law enforcement, military and economic assistance.

The U.S. will provide significant resources in support of the strategy; an estimated $2.2 billion over five years.

Levels and timing of U.S. assistance will be based on annual evaluation of Andean nation counter-narcotics performance over the previous year.

Projectized U.S. economic assistance cannot be turned on and off once activities are approved, which lessens control.

WEAKNESSES

The large number of quantitative measures of effectiveness to be used may make it difficult to evaluate Andean country performance.

The possible need to weigh effective counter-narcotics performance with unsound economic policies or vice-versa.

Question. How effective overall do you feel such a policy has been?

Answer. The Andean Counterdrug strategy is only recently underway so any appraisal of policy effectiveness is premature.

Question. What additional leverage and incentives would you suggest to increase the effectiveness of such a policy?

Answer. The incentives and leverage which have been built into existing international narcotics control (INC) programs have been very carefully considered so as to make them as effective as possible. Such incentives must be carefully tailored to meet the needs of each specific country involved.

Question. Can you cite any specific instances in which denial or the threat of denial of foreign aid was the decisive factor in a country's decision to take steps curbing international narcotics production or trafficking?

Answer. The annual certification process is the principal formal means employed by the U.S. to deny or threaten to deny foreign aid to a country. We believe this mechanism has influenced certain countries to take positive steps in curbing narcotics production and trafficking by publicizing their degree of cooperation or lack thereof with U.S. counter-narcotics efforts. In the case of Laos, for example, decertification by the U.S. in 1989 had a positive influence on subsequent actions by the Lao Government, which led to signing of a bilateral agreement with the U.S. in 1988 and opened the way for cooperation in law enforcement, crop substitution and demand reduction.

INTERNATIONAL NARCOTICS CONTROL: POTENTIAL FOR CROP-SUBSTITUTION PROGRAMS

Question. The President's drug-control strategy calls for increased economic assistance for Colombia, Peru and Bolivia over the next five years. Much of this assistance would be used to fund programs designed to promote the production of alternative crops to coca.

Many suggest that such programs are doomed to failure as no crops exist that could economically compete with coca, and that even if alternative crops could be produced, existing transportation and market infrastructures would be unable to facilitate their sales. For example, what business enterprise would fly an aircraft into the jungle to pick up bananas and transport them to the United States and elsewhere?

Where does the United States currently support some form of crop substitution or income substitution programs? Specifically in Latin America, what dollar amount is allocated for such programs for FY 1990 and FY 1991?

Answer. The U.S. (A.I.D. and State/INM) currently supports crop/income substitution programs in Pakistan, Bolivia, Peru and Laos. A new A.I.D.-funded activity is also about to get underway in Afghanistan. The following A.I.D. funding is planned for alternative development in and around the hard-core Andean coca-growing areas:

	Millions
Fiscal year 1990:	
Bolivia (Chapare Regional Development Project)	$12.0
Peru (Upper Hualaga Development Project)	1.5
Fiscal year 1991:	
Bolivia (Alternative Development Project) [1]	12.2
Peru (Upper Hualaga Development Project)	2.0

[1] Follow-on activity to Chapare Regional Development Project.

Question. Can you briefly describe the rationale behind such programs and how they work?

Answer. The basic rationale for U.S. income substitution-type programs is to provide alternative sources of employment and income to farmers engaged in producing coca/opium. Initial crop substitution efforts were primarily focused on replacing coca/opium with alternative agricultural crops. Since the areas where illicit crops are grown are often remote, inaccessible, insecure and poor, early crop substitution was expanded to include physical and social infrastructure, training and other direct assistance under a broad area development approach. As part of the Andean Counter-Narcotics Strategy, alternative development projects will be targeted towards hard-core coca areas, with the main emphasis and resources directed towards creating jobs, and income opportunities in adjacent areas. These activities are just one element in a broadly-based strategy aimed at generating alternative employment and sources of income throughout the economy.

Question. Have any major problems been encountered in administering these programs? If so, what do they tend to be?

Answer. In general, the relative remoteness, inaccessibility and insecurity of many coca/opium producing areas in Latin America and Asia serve to hinder implementation of effective alternative development programs. The cultivation of coca leaf and opium poppy are more profitable for farmers than any known alternative crop introduced to date. Likewise, a well-established marketing system already exists for coca and opium, while new marketing links need to be established for every new crop introduced. As government interdiction and enforcement efforts take effect, it is felt the farmgate price of coca/opium will decline, making alternative income opportunities more attractive.

Question. In which countries are such programs seen as successful, and how and in what terms does your agency measure success?

Answer. There has been some success with area-targeted counter-narcotics development in Pakistan and Thailand, where coupled with effective government enforcement/eradication. Recent indications in Colombia and Bolivia suggest that increasingly successfuly interdiction and eradication measures have resulted in a decline in the price of coca leaf to Bolivian farmers, which has caused many to agree to voluntary eradication of some or all of their coca crop and to seek information from government agriculture research stations and extension agents in the Chapare about alternative crops. Ultimately, the best measure of program success will be substantial decline or elimination of illicit production and transition of farmers to alternate crops/income opportunities.

Question. What is the economic impact of illicit narcotics production on the economies of the countries in which the U.S. has crop substitution or income substitution programs?

Answer. There is no data available on the impact of illicit narcotics production on Asian economies (e.g., Afghanistan, Pakistan and Thailand) where the U.S. has, is or will shortly be implementing alternative development programs. Available data indicates the following economic impact of coca on the three Andean countries:

	Bolivia	Colombia	Peru
Foreign exchange earnings (millions)	$500–650	$800	$700
GDP per capita	600	1,400	800
Value added as percent of exports	4–7	1.5–3	2.5–3
Coca/cocaine as percent of legitimate exports	25–45	15	26
Coca/cocaine employment as percent of active population:			
Direct	12	0.5	1.7
Indirect	6	0.2	0.7

Question. Some figures suggest that in Bolivia, for example, 400,000 of Bolivia's 6,000,000 people depend on cocaine-related income, and that the cocaine industry provides the Bolivian economy with an estimated $600,000,000 per year—more than all legitimate exports combined. Do you think the economic impact of illicit narcotics is of a similar magnitude in any of the countries in which the United States has crop-substitution or income-substitution programs?

Answer. Estimates vary on the economic impact of the cocaine trade on the three Andean countries. For Bolivia, the Country Team estimates that the coca industry generated $500–650 million in 1989, roughly 10–15 percent of official GDP. Of this amount, $150–280 million was fed back into the Bolivian economy, representing 4–7 percent of GDP and 25–45 percent of legal exports.

In Peru, we estimate a dollar flow of $700 million into the economy from cocaine earnings, roughly 3 percent of GDP and 26 percent of legal exports. Given Colombia's larger economy, the role of cocaine earnings is relatively smaller. Cocaine-related inflows in Colombia may represent 1.5–3 percent of official GDP and less than 15 percent of legitimate exports.

While important, opium is not believed to exert a similar impact on the economies of Pakistan and Thailand where the U.S. has supported narcotics-focused area development. Due to continuing political instability, the economic impact of opium on Afghanistan is less clear.

Question. What about Bolivia? What programs do we have there?

Answer. The U.S. Government has supported crop substitution and alternative development in coca growing areas of Bolivia since 1975. Current authorized life of project funding for the A.I.D. Chapare Regional Development activity is $38.5 million. A follow-on Alternative Development activity for the Chapare and surrounding areas is proposed at $60.0 million.

Question. What are our short-term and long-term anti-narcotics control goals in Bolivia?

Answer. Over the short term, the U.S. will press Bolivian leaders toward developing and implementing a national drug control strategy, containing interdiction, eradication, alternative economic development, and domestic demand reduction components in balanced measure, as well as initiating unpopular actions, such as forced eradication of illegal coca. Our long-term strategic goal is to develop an autonomous Bolivian institutional capability to regulate indigenous, licit coca cultivation and trade; eradicate illicit coca; reduce excess coca cultivation; and apprehend and imprison or extradite drug traffickers.

Question. Do you think our overall anti-drug efforts in Bolivia can be successful unless an attractive level of replacement income is provided to those who currently grow coca?

Answer. The success of U.S. anti-drug efforts in Bolivia will depend on a combination of effective law enforcement to disrupt the market for coca derivatives and reduce their price, and the creation of viable on-farm and off-farm income opportunities for growers, especially outside the major coca producing areas.

Question. Do you see any practical means for putting such replacement income into the pockets of the Bolivian farmer?

Answer. The multi-year program of economic assistance contemplated for Bolivia under the Andean counter-narcotics strategy, is designed to create alternative income opportunities for coca growers and others who disengage from participation in the coca economy.

Question. Even if the United States were able to subsidize the Bolivian farmers, what would keep the drug traffickers from always offering that extra dollar as an incentive to the farmers?

Answer. It is not the U.S. intention to subsidize Bolivian or other farmers, but rather to assist the GOP in providing viable economic alternatives to coca, mainly outside the hard-core coca growing areas. Given recent success of government eradication efforts in Bolivia and Colombia, the farmgate price of coca leaf to farmers in Bolivia has dropped below the cost of production, causing a shift to alternate crops, and in some cases, to migrant farmers leaving the Chapare altogether.

Question. Do you have any idea how much it would cost each year to subsidize the farmers with an attractive level of replacement income in those countries where the United States has crop substitution or income substitution programs?

Answer. We do not believe that subsidizing farmers is a feasible approach to eliminating coca/opium production in countries where the U.S. implementing alternative development programs. With an estimated 1,000,000 farmers in Bolivia, Peru Afghanistan and Pakistan alone engaged in illicit narcotic crop production, the annual cost of subsidizing them for not growing coca/opium would be staggering, and it would not solve the problem. The preferred approach is to strengthen law enforcement to disrupt the drug marketing system, followed with development efforts to induce farmers to abandon illicit production for viable alternatives.

Question. Do you think this question is an important one, or at least a relevant one?

Answer. The issue of providing farmers with viable income-generating alternatives to coca/opium production is critical to success of our U.S. counter-narcotics strategy. However, we do not believe subsidizing farmers is a feasible option.

Question. Can you provide this Subcommittee with a study that addresses this issue, and with the data we have requested on replacement income?

Answer. No recent study on this subject exists, nor are we aware of any data that has been requested of the State Department on replacement income.

EFFECTIVENESS OF INTERNATIONAL NARCOTICS CONTROL PROGRAMS IN PERU AND BOLIVIA

Question. When can we expect to see some solid results from drug-control or eradication programs initiated to date? Have our programs to date had a meaningful impact on the amount of cocain produced in Peru and Bolivia that is available for export?

Answer. The vigorous Colombian offensive has resulted in a general disruption of narcotics trafficking both in and outside of Colombia. While these operations have set the cartels off balance with Colombia, prices of coca leaf and paste have been depressed in both Peru and Bolivia as a result of these operations. In Bolivia, for example coca growers have eradicated 3000 hectares of coca this year, an amount already above the previous year's total. We expect that the funding and resources supplied to Peru and Bolivia under NSD-18 will allow these countries to emulate the Colombian success in disrupting narcotics trafficking.

Question. Have our programs to date been able to reduce *net* coca production in these two countries?

Answer. To date, U.S. supported anti-narcotics programs in Colombia, Peru and Bolivia have slowed the cultivation growth rate and have disrupted links between the growers and traffickers. The result is a substantial decrease in the price of coca at the farmgate. This is important to our effort to provide incentives to growers to get out of the illegal coca business and into legitimate activities. Our law enforcement programs, 1991 economic assistance, and the strengthening of institutions and economies are aimed at this objective.

Question. Have they at least been able to prevent net coca production in these countries from increasing?

Answer. There has been a slow down in the expansion of net cultivation in Bolivia only.

Question. Do you really think that after all these years it is still a realistic goal to seek net reductions of coca production in these countries?

[If answer amounts to "yes":] What is different now than before that would enable us to succeed? To what extent have you been assigned an impossible task?

Answer. The National Drug Control Strategy lays out a comprehensive approach toward reducing the narcotics flow, recognizing that a net reduction in the flow of drugs cannot be accomplished without a reduction in the demand for drugs in the U.S. Moreover, NSD-18 commits significantly more resources toward supply reduction than in the past. While a net reduction in coca production continues to be a long-term goal, we believe that the current integrated planning approach, and enhanced resources make a net reduction an attainable goal.

Question. Let us talk of the next three to five years. What percentage decrease in the net production of coca in these nations can we expect to see in the next three to five years, assuming we fund the programs you propose? What would be the best we could hope for, and how realistic are our chances of achieving such results?

Answer. A supply side reduction strategy, as planned in NSD-18, can only be successful and sustained if accompanied by an equally rigorous attack on the demand in the U.S. and other countries. Moreover, the expanded effort focused on the Andean region to dismantle drug trafficking operations can only be effective in the long term, if appropriate measures are taken in the surrounding narcotics transit countries to catch the spillover from concerted anti-narcotics operations. At this point, it is impossible to assign a meaningful percentage reduction number given that we are still in the early stages of implementing the strategy.

Question. Let us assume we achieve [witness' best estimate] a *50%* percent reduction in net coca production as you suggest, what impact would it have on cocaine use in the United States? Can you say for certain it would reduce cocaine use here at home?

Answer. As noted previously, a supply reduction strategy can only work to reduce cocaine use in the U.S. in concert with a vigorous demand reduction strategy.

Question. What percent reduction in net coca production in these countries would it take to reduce cocaine consumption in the United States?

Answer. Assuming an equally rigorous demand reduction strategy, a 50% reduction in the cultivation of coca ~~would~~ have a significant impact on the *availability* and price of cocaine in the U.S.

Question. Are any figures like this available? Have you ever requested any from other agencies? Do you think that this is an important question?

Answer. While this is an important question, it does not reflect the complex relationships between grower, lab operators, middlemen, traffickers, etc. A 50% reduction in the cultivation of coca in the three main producing countries can only be effective if the net reduction is not made up by cultivations established in other countries by trafficking interests. An expansion and continuation of the Andean narcotics strategy is already in the planning stages to meet this contingency.

Question. Assuming momentarily that nothing your programs do will be able to affect cocaine consumption in the United States, do you see any *other* positive benefits in your programs for these two countries or the United States, or for the host nations themselves? Would you please elaborate?

Answer. First, from the standpoint of U.S. demand, successful programs will make cocaine more expensive to U.S. users and potential users. A substantial redevelopment package is conditioned upon the three countries' performance on anti-narcotics activities and the implementation of sound economic policies. These conditions, as well as the economic funding that goes with it, will stabilize the Andean economies, and provide the necessary political will to support democratic values in the region.

ANTI-NARCOTICS POLICY IN THE ANDEAN REGION

Question. The Andean region is the source of virtually all the cocaine that reaches the United States, and hence the target of U.S. coca eradication and cocaine interdiction efforts. In Peru and Bolivia coca generates more foreign exchange than any of those countries' legal exports, up to about $1 billion a year. Most analysts believe that if U.S. anti-narcotics efforts were successful, there would be a sizeable negative impact on those countries' economies.

The FY91 budget provides $6.8 million in drug-related development programs in the Andes—$12 million for Peru, and $5.3 million for Bolivia. What else does the Administration propose to offset the loss of income and foreign exchange caused by U.S. anti-narcotics program?

Answer. The FY91 budget proposes $13.5 million in drug-related development assistance in the Andes—$1.5 million for the Upper Huallaga Development Project in Peru, and $12.0 million for an Alternative Development Project in Bolivia. In addition, the economic assistance component of the Andean strategy will include project assistance and policy reforms to generate jobs, income and foreign exchange throughout the economy together with fast-disbursing balance of payments assistance to finance productive imports and/or service of debt to the U.S. Government or international financial institutions.

Question. In 1989 the United Nations began a voluntary coca-substitution program in Peru which has attracted 20,000 participants, a surprisingly high number. In exchange for the U.N.'s technical advice on alternative crops, participating farmers agree eventually to stop growing coca. The program allows farmers to continue growing the lucrative coca crop on part of their land, however, to help finance the transition to other crops. A farmers' group lobbied the U.N. to sponsor the program, after it was rejected by both the U.S. and Peruvian governments. Why did the U.S. reject this crop substitution?

Answer. We believe the question refers to a proposal submitted to U.S.A.I.D./Peru by a farmer co-op group in Uchiza and not the U.N. project currently underway. The U.S. rejected the co-op proposal based on U.S.A.I.D.'s assessment that allowing farmers to continue growning some coca with a guaranteed market during their transition to other crop, could stimulate increased coca production. Further, it was felt that resources devoted to purchasing coca could be better used to develop alternative income opportunities.

Question. What is your opinion of the U.N. program?

Answer. The A.I.D. mission in Peru believes that the U.N. project has been useful. The project has maintained a non-U.S. presence in introducing alternative crop varieties. The activity has supported the construction of a $3.5 million cocao processing plant and most of the cacao is exported. It has supported useful studies of various market interventions, kept alive the idea of alternative crops and strengthened farmer morale. Finally, the project has reduced the number of hectares under coca production where it has operated.

Question. Based on the response to the U.N. program, do you believe the Administration should consider voluntary, gradual eradication programs in the Andes? Why or why not?

Answer. The U.S. currently supports a voluntary coca eradication program in the Chapare and adjacent areas of Bolivia. The GOB provides $2,000 per hectare to farmers who eradicate their own coca crop. In addition, farmers who voluntarily eradicate the majority of their coca crop qualify for U.S.-financed agricultural credit and extension services totalling $6,000 ($1,200/yr. over 4 years) for use in developing alternative commercial crops. The A.I.D. project also provides assistant to communities that have eradicated at least 30 percent of their coca, in the form of improved schools, farm to market roads, water supplies etc.

The U.S. supports this approach because farmers who voluntarily eradicate their coca require alternative income, and the availability of project services provide the incentive for farmers and commnunities to eradicate. To be effective, however, benefits must be perceived by the farmer as certain, immediate and direct.

Question. What is your assessment of current U.S. crop substitution and eradication policy?

Answer. The U.S. does not support crop substitution per se, but rather alternative development which includes assistance to farmers in hard-core coca growing areas, and creation of alternative sources of jobs and income opportunities in surrounding areas and throughout the economy. Success of the development component, however, depends heavily on the effectiveness of government enforcement efforts to disrupt the coca marketing process and drive down the price of coca leaf, making alternative development opportunities more attractive to farmers.

Question. In the coca-producing region of the Upper Huallaga Valley, Peruvian narcotics traffickers and guerrillas often cooperate, with the guerrillas providing protection in exchange for payments which fund their operations and arms purchases. How can the Administration keep U.S. anti-narcotics personnel operating in that region form becoming involved in counter-insurgency operations? How is the Administration assisting Peru in its counter-insurgency efforts?

Answer. In certain areas, counter-narcotics activities are threatened by insurgent groups whose control over the areas prevent any effective government action to combat narcotics trafficking, and whose activities are inextricably intertwined with those of the narcotics traffickers. In those cases, it is inevitable that counter-narcotics efforts will at times require counter-insurgency efforts to regain government control over certain areas. U.S. anti-narcotics personnel have not been involved in counter-insurgency operations—nor will they, since DEA advisors alone accompany police anti-narcotics squads, and U.S. military trainers are restricted to a training role and are prohibited from participating in field operations.

U.S. Policy Toward South America

Question. What is your assessment of the status of democracy in South America and whether it can survive in the face of deteriorating living conditions?

Answer. The 1980s are now commonly referred to as a "no growth" decade in South America and the economic aggregates for the region as a whole are grim. But the issue of economic growth and living standards has become linked to the prospects for democracy in each and every country of South America in virtue of the truly notable fact that all of them now have democratically elected governments. None of us would now be framing the question in quite the same way if over the same decade a great democratic transformation had not taken place.

The great challenge of the 1990s then is to secure the democratic gains of the previous decade by effecting an economic transformation as deep and as embracing as the democratic transformation of the previous 10 years.

Of course, the kind of change needed to turn things around must come from the countries themselves. That is why I am encouraged by the fact that a profound rethinking of economic premises and postulates is underway. Statist and mercantilist models have been discredited by the economic performance of countries which have turned to market-based, outward-looking economic policies (e.g. Chile). Newly elected leaders in South America (e.g. Menem in Argentina, Collor in Brazil, Rodriguez in Paraguay) are trying to implement such reforms. Countries (e.g. Bolivia, Venezuela, Uruguay) that have already embarked on this course are keeping to it. And, there is a consensus about what is needed that cuts across traditional political divisions. But, of course, the challenge lies in implementation because there are significant costs and real change takes time.

Democratically elected governments—and that is all the South American governments—can "deliver the goods." To be sure, governments do not generate wealth; people do. But governments can open up economies, cut unneeded restrictions on the private sector, and create opportunities for growth with benefits that reach to all sectors of society. The same openess competition that, politically, brought about a democratic revolution can bring on an economic turn-around to realize more fully the promise of democratic change.

Question. Is there any danger that the United States may concentrate on Central America as a greater immediate threat, and neglect the greater long-run threat in the much more populous and important South America?

Answer. In a word, no. Not only are these very different times from just a few years ago, but we are keenly aware that the circumstances are also very different in these two key regions of Latin America. Just a few years ago we considered the Sandinista government in Nicaragua to be a threat to democracy in the hemisphere, particularly to the struggling democratic government of El Salvador, and to the national security of the United States. Now, with the extraordinary results of the February 25 election in Nicaragua and the restoration of democratic rule in Panama, it is clear that the tide has shifted dramatically in favor of democracy, and by extension in favor of U.S. interests in the region. We see the situation in Central America now to be much more one of opportunity than of threat.

At the same time, we are very aware of the challenges and opportunities that face us in our relationship with the larger, more populous and economically much more important nations of South America. We intend to redress the imbalance that was the unintended result of intense U.S. concern about Central America, and in fact have already made significant strides in that direction. The President's summit meeting in Cartagena with the presidents of Colombia, Bolivia and Peru, at which for the first time in our history we addressed the narcotics threat in a direct, coordinated and multilateral way, is good evidence of this change of focus. With the three concerned governments we are now in the process of building on the agreements and commitments achieved at Cartagena, and I expect solid, quantifiable results in this struggle against narcotics in the very new future.

Obviously, there is still a lot to accomplish in South America. Newly emerging democracies in Paraguay and Chile must be nurtured. The progress that Peru and Bolivia have made in redemocratization, against the odds of tremendous economic problems, also must be sustained. We must work with the courageous new governments of Argentina and Brazil as they attempt to overcome the problems resulting from decades of mistaken economic policies and bad management of resources. And in Colombia, facing the twin threat of narcotics trafficking and leftist insurgency, we must make it clear that we support democratic government's struggle on both fronts, not just on the issue that concerns Americans so immediately, drugs.

Question. What is U.S. policy doing to strengthen democracy in South America? Given the shortage of U.S. resources at present, what can the United States do to support these fragile democracies in the face of economic distress?

Answer. Bilaterally and multilaterally, the United States works with the full array of policy instruments to support democracy in South America. What we do to help the Andean governments combat the traffic in illegal drugs, for example, is—as it must be—also supportive of democratic institutions. When we signal our opposition to coups attempts against democratically elected regimes—especially in concert with other democracies—we affirm our support for the democratic process.

Countries know that the quality of our relationship with them depends on their support for human rights, whether or not conditionality is written into law. In regional organizations like the OAS, we strongly support the work of the Inter-American Human Rights Commission. Through the Administration of Justice and Democratic Initiatives programs of AID and in cooperation with nongovernmental organizations like the National Endownment for Democracy we are engaged in long-term constructive efforts to support directly the building of democratic processes and institutions.

Your follow on question recognizes that economic stress runs high in many countries and that the people are looking to democracy to improve their living conditions.

There is unfortunately no quick fix for the myriad problems that face elected governments—an easy remedy whose costs we could underwrite. But even within resource constraints, we can help.

Trade makes a dynamic contribution to economic growth. But we must work to ensure that our markets are open to the products of South America. Of course, we are right to insist on access to Latin markets. The benefits of free trade are not limited to increased Latin exports. Our presence in their markets, whether through our exports or real investments, provides stimulus and know-how to indigenous enterprise and productivity.

Available aid resources have a farther reaching effect if used—as they are—to encourage much needed policy reforms. We note too that other industrial democracies have been expanding their roles in South America in the areas of trade, investment, and assistance, and we see that as a natural and positive development.

In the long run, the continuity generated by strengthened democratic processes and institutions contributes to economic development in which all can participate.

Question. What is your assessment of the adequacy of the Brady Plan for dealing with the massive foreign debt of South American countries? To what extent have these countries been successful in arranging Brady Plan debt reduction agreements with the commercial banks? What are the lessons to be learned from the Mexican debt reduction agreement? Are any new initiatives contemplated in dealing with the foreign debt of these countries?

Answer. As Secretary Baker answered on March 1, the strengthened debt strategy provides a positive framework for achieving more manageable burdens for a broad range of debtor countries across the globe. The strategy offers heavily indebted countries the prospect of realizing reductions in their debt and debt service obligations to commercial creditors, introducing new incentives and support for implementing and sustaining sound economic policies. The success of the strengthened debt strategy ultimately will be measured as it is implemented, on a case-by-case basis, by the ability of countries benefitting from the plan to sustain economic reforms and realize renewed growth. However, it can be noted that Mexico, Chile, the Philippines, Costa Rica, and Venezuela, all of which have reached agreements with their commercial creditors under some variation of the Brady Plan, account for 44 percent of the $259 billion in commercial debt owed by the original Baker 15 countries plus Costa Rica.

With respect to South American countries in particular, Venezuela recently reached an agreement in principle with its bank creditors on a range of options, including a cash buyback of Venezuela's debt, permanent debt and debt service reduction, temporary debt service reduction, and new money. Chile's buyback of commercial bank debt in November 1989 was financed by resources made available under the Brady Plan, and Chile's new government may seek additional arrangements. Uruguay is negotiating with the IMF toward a standby agreement which could serve as the basis for debt/debt service reduction. Ecuador is negotiating with its creditor banks. We also expect that Brazil's new government, which has taken office pledging—and following through with—massive economic reforms, will seek to benefit from the strengthened debt strategy. An agreement between Argentina and its creditors will only be possible after that economy stabilizes.

Mexico's breakthrough agreement with its commercial creditors generated well-known debt and debt service reductions benefits for that country, but, perhaps even more importantly, helped to improve the climate of investor confidence critical to the success of any economic program. The relatively long horizon of this package (four years compared to traditional 12-18 month reschedulings) contributes to the stability of Mexico's economic and investment climate, at the same time as it provides financial support in the form of reduced interest payments for Mexico's reform efforts.

The strengthened debt strategy is designed to be flexible in application, and has shown that it can respond to differing needs of specific countries and changing circumstances.

U.S. ASSISTANCE TO COSTA RICA, HONDURAS, AND THE EASTERN CARIBBEAN

Question. Although much of the decrease in assistance to Honduras for FY 1991 is in military aid, Honduras would still receive $41 million in that category compared to $37 million in development assistance. Given that economic socio-economic conditions in Honduras are dismal, with malnutrition reportedly increasing, and given that the Sandinista military can no longer be considered a threat, do you think there should be more of an emphasis on development and food assistance rather than military aid? Given the substantial amount of assistance to Honduras over the last ten years, what have been the major accomplishments of U.S. AID in Honduras in terms of helping the poorest sectors?

Answer. The $41.1 million aid level requested for FY 1911 is equal to that received ion FY 1989 and double that received in 1990, although the actual requirement, as shown in the Administration's Congressional request for fiscal year 1989 and fiscal year 1990 was over $60 million for each of those years.

It should be emphasized that the Administration's priority continues to be on economic, rather than military, assistance. The $41.1 million request level is 24% of the total foreign assistance request for Honduras, totalling $173.6 million; the other $132.5 million in economic assistance.

The $36.9 million level request in development assistance (DA) funds is higher than the actual FY 1990 level and approximately the same as the FY 1989 level. Together with food assistance under PL-480 Title I and Title II and section 416, DA funds have most immediate impact on the lives of the poorest segments of the population in Honduras.

Although Honduras is still one of the poorest countries in Latin America, the Government of Honduras has utilized U.S. economic assistance to bring about significant benefits to its people, particularly in the social sectors. For example:

Life expectancy increased from 53 years in 1972 to 65 years by 1989.

Infant mortality has dropped from 115/1000 in the 1970s to an estimated 60/1000 in 1988, due in large part to AID support to Honduran health services, food programs, and child survival activities.

AID supports immunization coverage for children under five. In 1988, immunization rates reached 83 percent against tuberculosis.

Reported cases of malaria decreased from 57,000 in 1982 to 23,000 in 1988.

AID supported education programs have contributed to a 20 percent increase in enrollment in primary schools in the last four years.

Nearly 30,000 land titles have been issued to rural families since 1982.

Contraceptive prevalence has incresaed from 27 percent in 1981 to 42 percent in 1988.

Question. Honduran President Rafael Callejas has taken a number of economic reform measures which had long been advocated by the United States, including a 100% devaluation of the lempira. Honduran workers have protested the measures in anti-government demonstrations. Will U.S. economic assistance help shore up support for the Callejas government in light of increasing popular protests against austerity measures? Do anti-government demonstrations in Honduras present a threat to the newly elected Callejas government?

Answer. U.S. economic assistance is vital to the success of the Honduran reforms, and therefore to the long-run strength of the Honduran economy. In that sense, U.S. assistance is important to President Callejas. However, it would be misleading to suggest that his government depends solely on our support. President Callejas was elected very recently by a large margin and remains very popular in Honduras. By most indications, his reforms are widely accepted as painful but necessary. Popular protest against austerity measures was foreseen by the Callejas government; thus far it has been moderate. We do not believe these demonstrations pose a serious threat to the government.

Question. What is the rationale for reducing economic assistance for Costa Rica for FY 1991? Why does the Administration's request for Costa Rica reflect a larger decrease in U.S. assistance than for any other Central American country?

Answer. Costa Rica is a valued Central American ally. The country's economic performance since 1986 has been strong. The level of $64.7 million in total economic assistance requested for 1991 represents a continuing decline from the peak level of $180 million in FY 1985. U.S. aid policy directs that aid levels reflect real economic needs. Declining aid levels to Costa Rica are a reflection of the country's steady progress in moving toward sustainable economic growth. In addition, FY 1990 funds contained a one-time U.S. contribution of $33 million to Costa Rica's commercial debt buyback scheme.

The U.S. economic aid program proposed for 1991 is designed to assist in supporting priority activities outlined by the Costa Rican Government. FY 1991 aid will support such activities as export development, natural resources, private sector development, and agricultural diversification. U.S. development assistance will also continue to be devoted to family planning, housing, the regional democracy and justice programs, and scholarships.

Question. In light of government changes in both Nicaragua and Panama as well as in Eastern Europe, will Costa Rica and Honduras have to compete for U.S. foreign assistance in future fiscal years?

Answer. U.S. foreign assistance funds are stretched even more thinly at present than in recent memory. There are a number of very important claims on these resources worldwide, and only limited availabilities. The administration will need to evaluate needs of all prospective aid recipient nations, and the economic assistance levels ultimately appropriated, along with earmarks, in order to allocate levels of aid.

Question. What is the rationale for declining U.S. assistance to the island-nations of the Eastern Caribbean? What has been the reaction of these nations to recent cuts in U.S. assistance? Of all the countries in the region, which countries have received the largest decrease in U.S. assistance? How much has been requested for Grenada for FY 1991? Please provide statistics showing a breakdown of how much each of the island-nations has received in economic and military assistance for the last five years and for the FY 1991 request.

Answer. U.S. assistance to the island nations of the Eastern Caribbean has declined because Congressional earmarking of foreign assistance funds has limited the Administration's flexibility in providing assistance to unearmakred recipients.

The reaction of the pro-Western, democratic Eastern Caribbean nations to recent cuts in assistance has been negative.

Economic assistance to the Eastern Caribbean is part of a regional program administered by U.S. A.I.D. in Bridgetown, Barbados. Due to the regional nature of the program, country-by-country statistics are not available.

EASTERN CARIBBEAN REGIONAL

[In millions of dollars]

	1986	1987	1988	1989	1990	1991 request
Economic assistance: [1]						
DA	23.7	29.7	31.7	18.9	17.4	17.6
ESF	25.6	21.1	1.0	10.2	0	10.0
Security assistance:						
MAP/FMSF		5.0	1.0	.5	0	4.5
IMET		.39	.4	.34	.45	.7

[1] Includes: Antigua, Monsterrat, St. Kitts, St. Lucia, Dominica, St. Vincent, and Grenada.

[2] Includes: Antigua, St. Kitts, St. Lucia, Dominica, St. Vincent, Grenada and Barbados.

U.S. POLICY TOWARD PANAMA

Question. Some economists have estimated that Panama will need as much as $2 billion over the next year to get the economy moving. What has been the reaction of the Endara government to the expected provision of $500 million in new economic assistance? What was the rationale behind President Endara's 13-day hunger strike earlier this month? What has been the reaction of the Panamanian business community to the announcement of $500 million in new economic assistance?

Answer. Panama recognizes that the U.S. Government alone will not provide all of the financial resources required to resolve the country's economic problems. Panama's leaders have expressed appreciation for the proposed $500 million second phase of the assistance package and they are looking elsewhere for complementary resources, including private investors. They are also placing special emphasis on using Panama's domestic resources efficiently. Panamanian Government officials stress, when talking about United States assistance, the importance of prompt approval. Without formal approval of the United States assistance package, the U.S.G. cannot lead a support group to help Panama clear its arrears with the international financial institutions. Furthermore, without United States assistance, Panama cannot achieve the level of investment the country needs to re-establish an acceptable level of growth.

President Endara's action was, as he described it, a lenten fast rather than a hunger strike. He sought to demonstrate, within the spirit of the lenten season, his sympathy for the many Panamanians who are suffering for lack of a job, adequate housing, et cetera. It should be noted that, during the entire period of his self-imposed fast, President Endara continued to maintain an active work schedule. His demonstration of concern for the poor, moreover, reportedly made a very favorable impression on the Panamanian public.

The Panamanian business community has acted rapidly to repair the physical, financial, and psychological damage it suffered during the past several years. It has quickly taken advantage of the credits made available as part of the first phase of our assistance program. Thus far, it has commented favorably on the proposed $500 million assistance program although, as one might expect, some would like the United States to provide more funds. As with the Panamanian Government, however, the private sector is most anxious that the United States quickly approve the assistance program. Businessmen believe when that happens and capital begins to flow, they will gain access to badly-needed credit, the Government will pay its bills and stimulate the economy, and international investors-financiers will regain their confidence in Panama's economic future.

Question. Panama's 67-member Legislative Assembly was installed on March 1, 1990, based on the electoral results from May 1989. How many seats will the government coalition control in the Assembly, and how cohesive is this ruling coalition?

Answer. The Government coalition has 27 seats for the Christian Democratic Party [PDC], 15 seats for the National Liberal Republican Movement [Molirena], and 9 seats for the Authentic Liberal Party [PLA]—a total of 51 seats. The leaders of the three parties—President Endara, First Vice President Arias Calderon, and Second Vice President Ford—have repeatedly stated their intention to work together in the new government; Ford recently told visiting U.S. legislators, "I can tell you categorically that we're in it for the long haul."

Question. How many seats will opposition parties control in the Legislative Assembly, and does the opposition plan to work within the political system?

Answer. The opposition Democratic Revolutionary Party [PRD], formerly controlled by strongman Noriega, has six seats in the Assembly, and the formerly Noreiga-controlled Labor Party [PALA] may be awarded one seat based on its nationwide vote total in 1989. Although it is too early to tell whether the opposition as a whole plans to work within the political system, two of the six PRD legislators showed up for the opening session of the Legislative Assembly and indicated their intention to participate; the other four, in an empty gesture, boycotted the session.

Question. How much support do opposition parties have in Panama?

Answer. For now, public support for the opposition is minimal. The former pro-Noreiga coalition of leftist labor unions and radical students, which played on resentment among the poor, no longer finds resonance in the public at large. However, any long delay in the provision of promised U.S. assistance would lead to frustration of widespread popular expectations. The opposition would almost certainly exploit such circumstances with nationalist, anti-U.S. appeals.

Question. When will new elections be scheduled for those seats where the results of the May 1989 elections are unknown?

Answer. On February 23, Panama's electoral tribunal presented credentials to 57 winners in the May 1, 1989, election. Ten seats could not be decided for various reasons, and runoff elections will be held at a later date to be announced—perhaps in May.

Question. What is the future of the new Arnulfist Party, the party of President Endara, which was not able to field legislative candidates in the May 1989 elections?

Answer. On April 28, the Arnulfista Party will launch a nationwide campaign to sign up members. Under Panamanian law, in order to gain official recognition and be authorized to field candidates in elections, a political party must have a minimum number of inscribed members—in this case, 19,252. The Arnulfistas expect to reach that level quickly. The Arnulfistas also plan to select as their new party President, Mireya de Gruber, widow of party founder and former Panamanian President Arnulfo Arias.

Question. What progress has been made in reestablishing Panama's judicial system?

Answer. The supreme court is functioning, albeit under difficult circumstances—it is located in temporary quarters, is in the process of reorganizing, and has suffered losses of case files. Lower-level judges and other judicial authorities are being named. Police are functioning and have received basic training.

Question. What type of support is the United States providing to help restore the judicial system?

Answer. The United States is providing training in the modernization and professionalization of the court system to include the introduction of new court administrative procedures and improved management procedures. We are also providing law materials and libraries. Our proposed program would also support the relocation of the supreme court and Panama City courts to a new building.

We are seeking also to help modernize and professionalize the public ministry through the introduction of such improved techniques as oral proceedings, case tracking, and other management information systems, as well as training of prosecutors and other ministry personnel. Attention will be given to developing new skills required by recent adoption of oral proceedings for certain kinds of cases, as well as the expected incorporation of the technical judicial police into the ministry. Some commodities will be provided.

The GOP is stressing the need for prefessionalization of the new civilian police force which is now subordinate to the Ministry of Government and Justice. Training and technical assistance is designed to emphasize community service and human rights as well as leadership and competent management. Basic police equipment—vehicles, radios, uniforms, laboratory equipment—are being provided.

We are supporting Panamanian efforts to improve civilian-police relations and to strengthen the understanding of a civilian government's role with respect to national security issues and control of public forces in a democratic government. The program will sponsor consultations from experts, conduct workshops and seminars for government officials and the public on these issues, and support studies and publications on the topic in Panama. As a complementary program, specially designed human rights courses will be offered to the public forces and governmental officials.

Question. Although the number of U.S. troops in Panama is down to its pre-invasion level of 13,600, the troops remaining are still involved in patrolling in Panamanian territory and assisting the new Panamanian Public Force in police functions. Specifically, what type of support is the U.S. military lending to the Panamanian Public Force?

Answer. At the request of the Government of Panama, United States military police and reservists with civilian police backgrounds are accompanying patrols of the Panamanian policemen in Panama city and are assisting in the precinct houses. United States special forces units are supporting the police in some rural areas. By accompanying police patrols and providing psychological, moral and management support, U.S. personnel help create a sense of greater security and professionalism.

Question. When will the new Panamanian Public Force be ready to maintain security on its own?

Answer. As soon as the Governments of Panama and the United States agree that the Public Force is fully capable of providing law enforcement services, the United States military will stop accompanying Panamanian police patrols. The United States Department of Justice is providing civilian law enforcement training under the Urgent Assistance to Democracy in Panama Act to develop the public force capabilities as expeditiously as possible.

Question. Is the U.S. military involved in providing any other type of support to the Panamanian Government?

Answer. Yes. United States military engineers are carrying out humanitarian civic action exercises to make urgently needed repairs to infrastructure in Panama, such as schools and roads, which were neglected under Noriega and are in marginal condition.

Question. Are civil affairs units of the U.S. military still lending support to the new government?

Answer. Some 10 to 15 civil affairs personnel are still in Panama operating with the national police. These U.S. military personnel are phasing out and are scheduled to depart early in May.

Question. On March 3, 1990, one U.S. soldier was killed, and 15 other U.S. servicemen and 12 Panamanians were injured in a grenade attack on a disco in Panama City. What is known about the perpetrators of this attack? Is there any evidence of armed groups, perhaps remnants of the old Panama Defense Force or the paramilitary Dignity Battalions, posing a threat to the stability of the new Panamanian government? What are the chances of other violent acts against U.S. soldiers or other U.S. citizens in Panama? Are there any signs of increasing anti-Americanism in Panama? Is there any anti-American sentiment linked with the role of U.S. troops in assisting the new Public Force in its police function?

Answer. The extensive investigation that has followed the March 3 terrorist act has not developed any definite information on, or leads to, the perpetrators of the attack. The investigators are reasonably convinced, however, that the attack was an isolated affair. They have found no evidence or indication that the attack was part of a broader terrorist campaign or that the perpetrators were members of a significant organization. We do not believe, therefore, that there is a major threat of violent acts against U.S. soliders or civilians. On the other hand, one cannot discount the possibility of further isolated incidents given the unsettled conditions in Panama.

Several reports have surfaced about possible armed groups that reject the authority of the Endara government. None of these reports has been verified. Moreover, they have all been about very small groups in remote areas of the country. Usually they are described as composed of men from the former dignity battalions or Panama Defense Force who have no support among the general public. Presuming the small armed groups exist, they evidently do not constitute a threat to the Government. However, a further deterioration of the economy or even an extended prolongation of the current recession would create a favorable milieu for all dissident political elements.

Indications are that the United States military forces and our military action of last December continue to be highly popular in Panama. There are no signs of growing anti-Americanism, although some Panamanians are clearly frustrated and disappointed with our failure to provide more assistance to date. The United States forces have developed increased favor among Panamanians who were highly concerned about a breakdown of law and order. They view the United States troops, who have essentially terminated their police activity but continue to accompany Public Force patrols, as a symbol and guarantor of security.

Question. Do you forsee a future role for the U.S. military in Panama beyond the year 2000 when the Panama Canal Treaty expires? Have you or other U.S. officials broached this issue with the new Panamanian government? If not, will this issue be brought up in the future? What is the Endara government's position on this issue? How is this issue perceived by Panamanians in general? What is your view of a role for the U.S. military in Panama after the year 2000?

Answer. The United States has primary responsibility for the canal's defense during the canal treaty's term. Beyond the year 2000 and the termination of the basic canal treaty, the United States will share with Panama permanent responsibility for maintaining the canal's neutrality under the companion neutrality treaty which will continue in force.

At the canal treaty's end our military presence will cease unless the two governments should agree otherwise.

The Panamanian Government has made clear its desire to resume a genuine partnership between our two sovereign nations regarding the operation and defense of the Panama Canal and we believe that the Panamanian people are strongly supportive. To that end, our two governments will consult closely as necessary. We have not, however, brought up the issue of a post-2000 presence with the Endara government nor have they with us. With a full decade to go in treaty implementation, it would be premature to address this issue especially with so many other issues of more immediate consequences on our agenda. As is the case with our other military base arrangements worldwide, we will assess our strategic interests and then consult with the host government prior to making a decision as to whether to seek an extension of our base rights. Such strategic assessments can only be made intelligently as we move closer to the termination of our current base agreements in the context of the overall security situation and our overall force posture.

Question. On March 3, 1990, President Endara announced the nomination of Gilberto Guardia Fabrega as the new Panamanian Administrator of Panama Canal Commission, replacing Fernando Manfredo who has served as acting Administrator since his appointment by President Bush on January 1, 1990. Will the nomination have to be approved by Panama's Legislative Assembly before it is sent to the United States? What is your impression of the nominee's qualifications for the Administrator's position?

Answer. The Government of Panama has forwarded to the United States Government the nomination of Gilberto Guardia as Administrator of the Panama Canal Commission as specified by the Panama Canal treaties of 1977. The treaty does not require that the Panamanian legislature approve the nomination. Mr. Guardia is a highly respected member of the international engineering community and president of a large construction firm in Panama. He worked as an engineer with the Commission early in his career. We have confidence in his ability to administer the Commission effectively as it faces the challenges of the next decade.

El Salvador Investigations and Human Rights

Question. Would you summarize the present status of the case involving the killing of the six Jesuit intellectuals at the Central American University (UCA)? How long will the current "investigatory" phase of the case take before it moves on to the "plenary" phase where the judge and defense explain in writing what the evidence shows?

Answer. On January 19 the judge opened the pre-trail or "investigatory" phase of the case, which can last up to 120 days. However, due to backlogs, insufficient personnel resources, and other reasons, it is common practice in El Salvador for judges to disregard the theoretical time limits for the different judicial phases. The judge in the Jesuit case has already indicated to our Embassy that he thought he would need the full 120 days. It is quite possible that he will require additional time.

During the investigatory stage the judge is taking statements from approximately 180 individuals who are believed to have pertinent information, reviewing the results of the investigation completed by the Special Investigative Unit (SIU), and ordering additional investigation by the SIU, as required. One of the areas being pursued is the question of the involvement of officers other than Col. Benavides, in the planning and/or cover-up of the crime. Another focus of the investigation is the effort to obtain evidence of Col. Benavides' responsibility other than the testimony of the other suspects, which under Salvadoran law are inadmissible as evidence.

When the judge believes he has all the necessary information and evidence, he will decide if the case can be raised to the trail or "plenary" phase.

Question. Over the years, a number of Salvadoran military officers have been implicated, and even charged, in a variety of human rights cases, notably the killing of the four churchwomen in December 1980 and the murder of Salvadoran and American land reform specialists on January 1981, but very few, if any, *officers* have been convicted by Salvadoran courts, and in some cases State Department officials or reports have asserted that bribery or intimidation were involved. Given this past history, what grounds do we have for believing that the officers involved in the killing of the Jesuit priests will be convicted?

Answer. I do not underestimate the difficulties El Salvador faces in ensuring that all those who violate human rights, including members of the military, are prosecuted, convicted, and punished. Nonetheless, there has been progress in improving the military's accountability to the rule of law. The Jesuit case illustrates that progress. The Special Investigation Unit (SIU) that developed the evidence that resulted in the arrest of eight members of the military for the crime is composed of investigators on detail from the security forces and is commanded by an army officer. The quality and thoroughness of the SIU's work has been evaluated and praised by professional investigators from the United States, the United Kingdom, and Spain. The SIU is now focussing its investigation on the possible involvement of other officers in the planning and/or cover-up of the killings.

The military high command has supported the Salvadoran Government's efforts to prosecute this case. A military honor board was formed for an internal review of the evidence and concluded that there was sufficient proof to recommend turning the accused over to the civilian judiciary for prosecution. The high command has cooperated with the SIU throughout the investigation. They understand, we believe, how crucial a successful prosecution of this case is to continued U.S. assistance to El Salvador.

Question. What is your reaction to the Washington Post story, on Feb. 22, 1990, that Colonel Guillermo Alfredo Benavides, the colonel charged with ordering the murder of the Jesuit priests, is being held in a luxury apartment in the National Police headquarters, rather than in a prison cell; that he has been seen in a luxury hotel owned by the military on the Pacific Coast; and that he has received regular visits from fellow members of the Tandona, the large military academy class of 1966 that presently holds most top military command positions?

Answer. There were unconfirmed press reports that Col. Benavides was receiving special treatment at National Police headquarters and that he had been given weekend leave to visit the beach. The Secretary called President Cristiani to convey our strong objection to preferential treatment for the accused. The Salvadoran military high command has denied that Col. Benavides was permitted to leave police headquarters on weekends. They also confirmed that Col. Benavides and the other suspects are being held in separate quarters. As they explain it, there are no separate military prison facilities in El Salvador and military prisoners cannot be mixed with the general prison population, which includes suspected FMLN guerrillas, for reasons of their own security. It is possible that Col. Benavides has received visits from fellow officers. We know that his family has been permitted to visit him, as is the practice with other prisoners as well.

Question. Since the early February press reports of a meeting of the Salvadoran high command on the evening the Jesuits were killed, and a meeting the following morning where intelligence officers applauded when informed that Jesuit priests at the Central American University had been killed, are you confident that all parties have been charged who were involved in the killings, or in the cover-up of the murders?

Answer. The SIU's investigation is continuing and is now in the process of looking into the meeting held on the night before the killings. As far as I am aware, no one has suggested that the fact that intelligence officers may or may not have welcomed the news of this horrible crime is in itself relevant to the investigation.

I am not able to offer an opinion as to whether all those involved in the murders, whether in the planning, execution, or any cover-up, had been identified, since the investigation is still going on. While I would not dismiss the possibility that other officers may have been involved, our Embassy in San Salvador, which has been closely monitoring the case, has not yet seen any evidence that indicates the involvement of other officers. I emphasize, however, that this issue is still being examined in the on-going investigation.

Question. What is the status of investigation of other recent politically-motivated killings, presumably committed by rightwing and leftwing extremists? These include the killing of 10 union members when the headquarters of the anti-government National Federation of Salvadoran Workers (FENASTRAS) was bombed on October 31, 1989; the killing of three regional workers of Ruben Zamora's leftist Popular Social Christian Movement (MPSC) in Sonsonate on November 6, 1989; the killing of Maria Isabel Casanova Porra, the 23-year-old daughter of an active duty Salvadoran colonel on October 17, 1989; and the killing of former Supreme Court Chief Justice Francisco Jose Guerrero on November 28, 1989.

Answer. FENASTRAS union were bombed by unknown assailants on October 31. Ten were killed in the blast, including FENASTRAS secretary general Febe Elizabeth Velasquez, and 30 wounded. FENASTRAS, UNTS, and the FMLN all blamed the Armed Forces and the Government for the bombing.

President Cristiani called for an investigatory commission to look into the crime, but FENASTRAS initially refused to permit the Special Investigative Unit (SIU) to conduct a physical examination of the site or the bodies. An FBI explosives incidents expert was made available and along with SIU personnel visited the site on November 8 after it had been cleaned up and much evidence taken away.

In January and in February, FENASTRAS leaders told Department and Embassy San Salvador officials that they had been encouraged by the speed and professionalism of the SIU investigations of the killings of the Jesuit priests, and that they intended to cooperate with the SIU's investigation of the FENASTRAS bombing. To date, however, they have continued to refuse to cooperate. The investigation remains open but is stalled.

Maria Casanova Porra was killed on her birthday while on her way to aerobics class. Her car was riddled with more than 50 AK-47 rounds. FMLN urban commandos admitted responsibility for the crime. The investigation of the crime has not yielded any leads.

Former President of the Supreme Court of Justice Francisco "Chachi" Guerrero was killed on November 28 as he rode to work. One of the perpetrators was captured; another was killed by Guerrero's bodyguards; a third escaped. The captured killer admitted that he was an FMLN urban commando. The escaped killer has not been found.

The National Police conducted an investigation into the killings of the three MPSC workers on November 6 in Sonsonate. The investigation revealed some inconsistencies in the stories of some of the participants, but apparently no firm leads were developed.

Question. In the last few years the "political space" in El Salvador has seemed to widen, with various leftists returning to engage in political activity, most notably the leftist parties allied with the guerrillas which formed the Democratic Convergence (CD) and campaigned openly for a negotiated settlement of the conflict in the March 1989 election. Since the guerrillas' November offensive, the political space has diminished, and many activists have fled or gone underground, alleging that the government is engaged in a campaign of harassment against church, union, relief, and humanitarian organizations which have been characterized as FMLN front by the government. What is President Cristiani doing to indicate that the space may open up again? In what ways is he indicating that church, union, and humanitarian organizations may function in El Salvador, and that foreign workers (some of whom were expelled) may return to El Salvador? Is he making efforts to indicate that the efforts of non-combatants caught in the middle, like the churches, the parties of the Democratic Convergence, etc., are free to engage in legitimate political activity in El Salvador? Is President Cristiani contemplating in the proximate future the termination of the state of emergency with its extended periods of unreported detention?

Answer. President Cristiani was very concerned by the charge that his government had a policy of harassment of church and relief organizations and went to great lengths to personally meet with church leaders, both in El Salvador and in the United States, to address their concerns. The number of church and humanitarian organizations raided and/or searched by the security forces during the FMLN offensive was relatively small and I believe that virtually all of them have resumed operation. The Salvadoran Government continues to issue visas to American church and relief workers who can establish that they intend to carry out legitimate, non-political work. In at least one instance, an American who was arrested and then ordered deported obtained a visa and visited El Salvador recently.

President Cristiani has been equally concerned about the leftist political parties and the threats to their security following the offensive. At President Cristiani's direction, the Salvadoran military has cooperated with one party in the CD to fulfill the party's specific requests regarding police protection and other measures. Similar protection and assistance were offered to a second leftist party, which declined the offer. The state of exception, imposed in November by the Legislative Assembly in response to the FMLN offensive, was renewed by the Assemby four times. It expired on April 12 and all constitutional guarantees have been restored. However, the provision which extended the police detention period from three to 15 days, had been removed earlier, on March 9.

Question. Concern was expressed about the use of air power by the Salvadoran military to dislodge guerrillas during the November offensive, and according to press reports, at least six persons were killed on February 11, 1990 when the Salvadoran Air Force bombed a settlement of former Salvadoran refugees at Corral de Piedra. What is your reaction to these reports, and what is the justification for providing sophisticated air power to El Salvador? Would you explain specifically the purposes for which FY 1990 military aid is being used, and the purposes for which the requested FY 1991 military will be used in El Salvador?

Answer. On February 11, approximately 100 FMLN guerrillas attacked a Salvadoran Armed Forces (ESAF) patrol in the vicinity of Guancorita in Chalatenango department. Approximately 300 returnees—Salvadorans recently returned from Honduras—live in Guancorita, also known as Coral de Piedra. The ESAF patrol called in the Air Force to disperse the guerrillas. During the course of the battle, a rocket from an attack helicopter hit a cinder block house where some two dozen returnees were sheltering. The resulting explosion killed five civilians (four children) and wounded 15 (12 children).

The Salvadoran government has publicly expressed its deep regret over the loss of life in the incident, and directed the U.S.-trained and -equipped Special Investigative Unit, which broke the case of the killing of the Jesuits, to investigate. On February 17, the government announced that the SIU had determined that an Air Force rocket had killed the civilians. In assuming responsibility for the tragedy, the ESAF emphasized that the rocketing was accidental. The government announced that it would compensate the families of the victims for their loss. We profoundly regret this accidental loss of innocent lives. Military assistance to El Salvador, including for FY 1990 and FY 1991, is provided to help the democratically elected government defend itself against the Marxist-led insurgency. Air assets, including transport and attack helicopters and attack fixed-wing aircraft, are used by the Salvadoran Armed Forces to address guerrilla attacks.

Question. What is your assessment of the prospects for a negotiated settlement of the conflict in El Salvador? Does the United States favor a negotiated settlement in the country? In what ways is the United States making it clear that we support a negotiated settlement? Are we fully supporting the appeal by the Central American presidents in December 1989 that the UN Secretary General seek to get the parties to return to negotiations? What signposts could we use to determine that the Cristiani government and the FMLN are acting in good faith, with all seriousness, to seek a negotiated solution?

Answer. We continue to support and encourage the Salvadoran Government's pursuit of a negotiated end to the war. We are very hopeful that the current round of peace talks, scheduled to formally open on May 3, under UN auspices, will lead to a permanent and peaceful resolution. We believe that the Salvadoran Government is equally hopeful and committed to this effort. Even before his inauguration President Cristiani pledged to seek an unconditional dialogue with the guerrillas. The UN's role in reactivating the peace talks has been invaluable. Continued UN involvement will no doubt contribute to the likelihood of a subsequent agreement. Both sides have already taken steps that signal a desire to end to violence. As a sign of good faith, the Salvadoran Legislative Assembly allowed the state of exception, imposed in November in response to the FMLN offensive, to lapse, with the agreement of the Salvadoran military. The FMLN has said it would halt its attacks against civilians and certain economic targets, although both continue to be attacked, albeit at lower levels. These are promising developments.

Question. After a decade of U.S. support for land reform in El Salvador, how would you assess the results? What plans does the Cristiani government have for modifying the land reform?

Answer. The land reform in El Salvador responded to an explosive social issue. From the social perspective, it has been reasonably successful. It resulted in the transfer of 23% of the arable land to formerly landless peasants, benefitting some 525,000 people. Nonetheless, there remain an estimated 150,000 landless families. The Salvadoran Government, with support from the Agency for International Development, is attempting to increase the number of beneficiaries.

From the administrative perspective, there has been significant progress. Former landowners have been compensated, except in about 50 cases still pending in the courts. Titling under Phase I, which affected the largest holdings, is virtually complete. Titling under Phase III (the Land to the Tiller program), which involves over 47,000 potential titles, should be completed by mid-1991.

The next step in the process is to given the owners of the land true rights of ownership. Under current law, agrarian reform beneficiaries can neither transfer their land to family members nor sell their parcel. Phase I cooperatives are run essentially as collective cooperatives while individual members might prefer other arrangements, including parcelization. At our urging the government is discussing draft legislation with campesino groups and other interested parties.

President Cristiani has vowed to "reform the reform" by increasing production on agrarian reform farms, as well as by increasing the number of beneficiaries. As previously mentioned, the government has drafted legislation which, among other things, would grant cooperative members the right to self-determination; i.e., they could vote on how they want their farms run—as service cooperatives or as individual parcels. The draft legislation would also permit all land reform beneficiaries to transfer their land to family members or sell it to other small farmers, but it would not permit resale to former landowners or the reconcentration of large holdings.

To increase the number of agrarian reform beneficiaries, the government is continuing a program begun under the previous administration to distribute unutilized or underutilized agrarian reform lands to landless families. In addition, the government plans to establish a land bank which will be able to distribute land to approximately 3,000 beneficiaries a year.

U.S. Economic and Military Assistance for El Salvador

Question. In the event that aid to El Salvador wer cut, or withheld pending action on certain human rights conditions, it might be important to know how much aid has been obligated or dispersed. Would you tell us how much of the ESF and military aid for El Salvador for FY 1990 has been obligated at present? How much ESF and military aid for El Salvador is in the pipeline—i.e, undisbursed—for FY 1990, and for previous fiscal years?

Answer. As of March 31, FY 1990 ESF obligations included only $9.7 million in FY 1989 ESF carryover for the Public Services Improvement Project. No FY 1990 ESF monies have been obligated to date. The ESF pipeline, as of March 31, was $151.7 million, all of which is project assistance.

Currently, $60 million in military assistance to El Salvador has been obligated, leaving approximately $19.6 in funds unobligated. As of February 15, 1990, $11.5 of the obligated funds were committed.

Question. What have been the concrete results of AID's support for judicial reform in El Salvador through the Administration of Justice program? Would you summarize the recent GAO report on the Administration of Justice program, and indicate any differences that AID or the State Department have with the report? While some progress has been made in investigative techniques and provision of court equipment and training, when do you expect to see progress in efforts to amend the Solvadoran legal code to make it easier to convict human rights offenders? When do you expect additional action in the case against military officers for the killing of the Jesuit priests? What signposts would you look to as evidence that we are making progress in judicial reform in El Salvador?

Answer. The Judicial Reform Project in El Salvador supports a legislative drafting commission (CORELESAL), the Special Investigative Unit and a variety of activities in the area of judicial administration and training. In addition to this project, El Salvador participates in regional administration of justice activities through the U.S. Latin American Institute for Prevention of Crime and Treatment of Offenders (ILANUD) and the International Criminal Investigative Training Assistance Program (ICITAP).

Each of these activities has had some success in its own terms—new laws have been enacted, judges and investigators trained—but the most important result has been to demonstrate that things can change with the appropriate impetus. Salvadorans are now looking for ways to improve the justice system. For example, the Supreme Court proposed last year that the project finance teams of judges to go from court to court to assist with case backlogs. Among the overdue cases that are being resolved in this fashion are those of individuals who have been in pretrial detention longer than the maximum sentence that could have been imposed had they been convicted. Getting lost in the penal system in this fashion is a common problem throughout Latin America, but one which can be resolved with a concerted effort.

The GAO report discussed the Judicial Reform Project only. It found that the project has had a positive effect on the Salvadoran justice system by helping improve its efficiency, investigative capabilities and professionalism and recommended against its termination. The Department strongly concurs in this recommendation. Our comments on the report will be published with it.

While several cases in El Salvador have highlighted the inadmissibility of codefendant testimony as a potential obstacle to conviction, the more serious obstacles still seem to lie in the lack of investigative professionalism and lack of collaboration among judges, prosecutors and police. There is simply no practice of developing criminal cases in El Salvador utilizing all available evidence. The Revisory Commission for Salvadoran Legislation (CORELESAL) is drafting amendments to the code of criminal procedure to facilitate trails and will be considering the issue of codefendant testimony specifically. Both the Judicial Reform Project and ICITAP are attempting to bridge the gap between police investigators, on the one hand, and judges and prosecutors, on the other, so that all criminal cases will stand a better chance of being resolved.

The Jesuit case is still in the investigative phase, which means that the judge is receiving evidence and ordering additional investigation, if required. When he has received evidence sufficient to support a determination that there is reasonable cause to believe that specific defendants committed the crime in question, the case will go to trial.

Judicial reform in a continuous process which encompasses a broad array of actions. It requires committed individuals in the public and private sectors working together to assess problems and implement desired changes. The Judicial Reform Project and other administration of justice activities in El Salvador have enabled and encouraged Salvadorans to take responsibility for their system of justice. Their heightened interest and activity, and the active support of the Government of El Salvador, are both prerequisites for judicial reform and evidence of progress toward that end.

In the criminal justice area, we should be looking for the resolution of more cases, both common and uncommon, on the basis of physical evidence. We should look for the institutionalization of proper crime scene procedures. For example, the fact that the SIU began to collect evidence from the scene of the recent Jesuit murders within hours of the discovery of the crime marks a decided change from other high profile cases such as San Sebastian where evidence was destroyed before the SIU was even assigned to the case.

In other areas, we should be looking for signs that the justice system is being made more accessible to all members of society and meaningful as a way of resolving disputes and protecting individual rights. For example, the Revisory Commission has proposed amendments to the Family Code which the GAO found was a high priority for resolving recurring social issues in the country. The international interest in human rights offenders should not be allowed to obscure the need for changes in other areas of substantive law or practice to restore public confidence in the legal system, the overall goal of judicial reform.

GUATEMALA MILITARY AID

Question. For several years the Administration defended the $9 million level for Guatemala, as importantly symbolically. An increasing level of military aid was supposedly required to strengthen General Gramajo's position with dissident elements within the Guatemalan armed forces. What happened to that priority in the allocation process?

Answer. In FY 90 due to the combined results of underfunding and earmarking we were only able to allocate $2.8 million for Guatemala while accomodating needs in other countries of the Hemisphere. The FY 91 CPD requested a modes increase to $5 million to enable us to also maintain small but important programs in the Caribbean.

We feel that it is still very important to provide this limited assistance to Guatemala for basic materiel and training for officers in the United States. The assistance is only a very small portion of the Guatemalan military budget but it provides us with some influence in working with those officers who support civilian government and are committed to democracy. Guatemala has now had four years of civilian rule and we wish to encourage this form of government as a permanent one.

GUATEMALA

Question. The U.S. Ambassador to Guatemala was recently recalled to Washington. The Ambassador apparently made a speech which was very critical of the Government's ability to control human rights abuses.

Recent reports indicate an increasing level of violence, in general, in Guatemala and in particular an increase in violent attacks on foreigners. The office of the International Red Cross was recently bombed, U.S. citizens have been attacked and a U.S. nun was abducted and tortured. What can you tell us about the recent wave of violence?

Answer. The present wave of violence began last summer with a wave of bombings aimed at frightening the populace and damaging infrastructure. The bombings have continued since on an intermittent basis. In addition, there have been assassinations of major political and business figures and a rash of kidnappings and murders. Though there have been some incidents directed at foreigners such as the bombing of the offices of the International Red Cross, the stabbing of three Peace Brigadists and the kidnapping of Sr. Ortiz, most of the violent acts are directed at Guatemalans.

The violence appears to be the work of political extremists of both the right and the left. Their aim appears to be to undermine civilian government and to disrupt the election process as the country moves to Presidential elections in October 1990.

Question. What has the U.S. done to investigate these incidents?

Answer. As you know, we do not have the authority to investigate incidents in Guatemala. Rather, we work with the Government to ensure that cases are properly investigated.

Due to the lack of movement on recent cases of human rights abuse, the Secretary of State temporarily recalled our Ambassador for consultations in March. After an absence of one week, Ambassador Stroock returned to post and met with President Cerezo to give him a letter of concern from President Bush.

President Cerezo has formally indicated to us that his government will be taking a number of steps to investigate outstanding cases, including the ones you mentioned, and to strengthen the rule of law.

As a first step, the GOG is establishing a new investigative police unit under the Attorney General to be charged solely with investigating cases of human rights abuse. The team will include policemen trained under the AID funded ICITAP Program.

In addition, the Government of Guatemala plans to send to Congress legislation to revise the penal code and plans to provide security for investigators and judges so that they can carry out their jobs without fear of retribution. We also expect to receive the results of the preliminary investigation of the murders of Hector Oqueli and Gilda Flores, as well as a list of army personnel who have been prosecuted for human rights abuses.

We are still discussing other meassures with the Government of Guatemala.

Question. What has the FBI done to assist the Guatemalan in these investigations?

Answer. The GOG has not formally asked for FBI assistance in the cases of the bombing of the office of the International Red Cross, the stabbing of the Peace Brigadists or the abduction of Sister Ortiz.

In light of the possible violation of U.S. laws on hostage taking and assault of U.S. persons abroad, the FBI has requested to speak to Sr. Ortiz. The purpose of this interview is to obtain the full facts on the case.

Question. Have the Guatemalans cooperated with them?

Answer. The FBI's request to interview Sr. Ortiz is to determine whether there has been a violation of U.S. law, not to assist in the Guatemalan investigation. The Government of Guatemala has not requested FBI assistance in this case.

Question. To what extent do you think that incidents were politically motivated?

Answer. We believe that a number of the incidents of terrorism and human rights abuse which have recently occurred in Guatemala were politically motivated. The guerrillas have been behind some incidents and have taken credit for several bombings. Other incidents, including the kidnapping of ten and the murders of five San Carlos University Students, the murders of Hector Oquelli and Gilda Flores, the bombings of the offices of the International Red Cross and of the International Peace Brigades and the stabbing of three Brigadists also appear to have been politically motivated, although there are no leads as to the specific perpetrators.

Question. Specifically, was the FBI sent to assist in the investigation of Hector Oquelli (the FMLN leader who was recently murdered in Guatemala) and to what extent did the Government of Guatemala cooperate?

Answer. President Cerezo did formally request FBI assistance in that case, and that agency has provided forensic law enforcement assistance. The Government of Guatemala cooperated in the FBI review of the evidence available. So far, however, the Guatemalan government has developed no leads on the perpetrators of this crime. We expect to receive in the near future a report on the preliminary investigation of the incident.

HONDURAS ECONOMIC PROGRAM

Question. Congress has recently been notified of your intention to disburse $120 million in ESF funds to Honduras. ESF to Honduras has been withheld for almost two years pending the implementation of an economic reform program. Recently, a new president took office. Explain to the Committee the basis for releasing the $120 million. Outline the specific steps taken by the Hondurans in their economic reform plan. Have they agreed to let their currency rate of exchange float, or will it remain at the officially fixed rate?

Answer. Fiscal Year 89 ESF funds for Honduras totaled $85 million. $15 million of this amount was tied to projects and was disbursed in Fiscal Year 89. The remaining $70 million was withheld for about one year and was obligated in March 1990, along with $60 million in Fiscal Year 90 ESF funds. Of the new total of $130 million, $40 million was disbursed on April 2, 1990, with the remainder to be disbursed later this year.

The funds were released following the announcement on March 2, 1990 by President Callejas of sweeping economic reforms to be implemented immediately. These reforms had five principal goals: Reduce substantially the central government fiscal deficit, reduce the role of government bureaucracy in the economy, make the budget process more transparent, reduce the tariff regime, and rationalize the exchange rate.

Among the specific steps taken: (a) The Government abandoned the fixed exchange rate, which existed over 70 years, and moved the lempira to a crawling peg system. The lempira was initially set at 4.1 to the dollar (near the parallel market rate) and will be periodically adjusted according to demand. (b) The Government also announced plans to eliminate at least one ministry and consolidate others, along with measures designed to reduce both the number of Government employees and the regulations they oversaw. (c) The Government announced a budget deficit target of only 5 percent, about half that of the previous year, to be achieved through higher taxes and lower Government spending; at the same time measures were announced for temporary subsidies to ease the transition, aimed especially at the poor and at unmarried mothers. (d) Measures were also taken to stimulate exports and raise the cost of imports, both via the new exchange rate and via a new tariff schedule. (e) Many subsidies previously hidden in the budget have now either been eliminated or made explicit.

U.S. Bases in Honduras

Question. Honduras recently announced their intention to convert Palmerola Air Base (the main location of U.S. troops for the past 7 years and the location where $20 million in U.S. military construction funds were spent to upgrade the runway) into a civilian airport.

The U.S. is also in the process of negotiating a bilateral agreement with the Hondurans dealing with the future of U.S. semi-permanent bases. Among other things the draft agreement specifies that the U.S. will turn over to Honduras, all of the facilities it currently occupies. The U.S. has invested over $40 million in Honduras in construction in the past seven years.

What specifically does the proposed bilateral agreement call for in the way of the U.S. turning over facilities to the Hondurans?

What is the U.S. view of making Palmerola Air Base a civilian airport?

What is the precise status of the bilateral agreement with Honduras?

Answer. The United States does not have any bases in Honduras. Approximately 1,200 United States personnel comprise Joint Task Force Bravo, stationed at the Honduran base at Soto Cano.

Although newspapers reported plans to convert Soto Cano Air Base, formerly known as Palmerola, to a civilian airport, this was in fact only one of several proposals whose origin lay in the need for a safer airport than Toncontin, which presently serves Tegucigalpa. Another proposal suggested building a new airport in Tegucigalpa. The proposal which appears to have the most serious consideration at present would make the international airport in San Pedro Sula the country's only one, leaving Toncontin as a national airport with shuttle service to San Pedro Sula. We do not believe the Soto Cano proposal is under serious consideration.

The billateral agreement you refer to is Protocol III, one of three protocols negotiated between Honduras and the United States in order to augment the bilateral military assistance treaty of May 1954. Protocol I addressed legal jurisdiction over United States military personnel in Honduras; it entered into force on April 9, 1987. Protocol II addressed cooperation in combined military exercises in Honduras, and entered into force on May 23, 1989. Protocol III has not yet been approved by the Honduran Congress; President Callejas has told us it remains under discussion within his government.

Protocol III provides for full consultation between the United States and Honduras regarding construction or improvement of military installations and sites in Honduras. Honduran authorities would have the right to approve in advance any permanent or removable construction. Permanent structures would become Honduran property, while the United States would retain use rights. Protocol III also addresses the carrying of weapons by United States personnel, use of Honduran utilities and services, application of Honduran taxes and duties, Honduran access rights, and United States contributions to maintenance and repair costs. Honduras would retain the right to approve the level of United States military presence in Honduras. A draft copy of Protocol III is attached for your reference.

OUTLINE

Protocol III to the Bilateral Military Assistance Agreement of 20 May 1954 between the U.S. and Honduras concerning Construction, Improvement and Use of Honduran Military Installations and Sites

- This protocol provides for full consultation between the USG and GOH regarding construction or improvement of military installations and sites in Honduras. It has not yet been approved by the Honduran Congress but should be discussed in early 1990.

- Protocol I addressed legal jurisdiction over U.S. military personnel in Honduras; it entered into force on April 9, 1987. Protocol II addressed cooperation in combined military exercises in Honduras, and entered into force on May 23, 1989.

- Under Protocol III, Honduran authorities must approve in advance any permanent construction (including permanent structural improvements). Removable construction must have prior authorization from the relevant Honduran base commander. Permanent structures become the property of the GOH, while the USG retains use rights.

- Honduras will make available the necessary land, easements, and rights of way. The U.S. will provide compensation in the case of privately-owned property.

- The U.S. may choose its own personnel to perform construction, maintenance, etc. but should use as many Hondurans as possible. Non-Hondurans will not be subject to Honduran taxes and duties. The U.S. retains title to all movable property brought into Honduras for activities covered by this protocol; Honduran taxes and duties do not apply as long as the property is ultimately exported or transferred to the GOH. The GOH will facilitate entry of U.S. personnel; third-country nationals remain subject to Honduran immigration regulations.

- U.S. personnel may carry weapons under certain circumstances. Storage and handling of U.S. weapons systems will be governed by mutual agreement.

- The USG may use Honduran utilities and public services where appropriate. Maximum use is to be made of Honduran goods and services when purchases are required.

- Installations and sites are under Honduran command; U.S. forces remain under U.S. command. The Honduran commander has access rights. Access to classified areas will be governed by mutually-agreed procedures. Honduras is responsible for protection of installations and sites from external threats.
- When U.S. forces use installations or sites, the USG will contribute to maintenance and repair costs via a mutually-agreed formula.
- The GOH retains the right to approve the level of U.S. military presence in Honduras and to approve/reject any deployment of U.S. forces in Honduras. The GOH must be advised of the particulars of each deployment in advance.
- Additional points address use of air and sea ports in Honduras by U.S. craft; obligations under the Treaty for Prohibition of Nuclear Weapons in Latin America; compensation for legal claims; and sharing of agreed-upon benefits (a classified appendix relates to this).

drafted: ARA/CEN:CJSandrolini
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PROTOCOL III TO THE
BILATERAL MILITARY ASSISTANCE AGREEMENT
OF 20 MAY 1954 BETWEEN
THE GOVERNMENT OF HONDURAS,
AND
THE GOVERNMENT OF THE UNITED STATES OF AMERICA
CONCERNING THE
CONSTRUCTION, IMPROVEMENT AND USE
OF HONDURAN MILITARY INSTALLATIONS AND SITES, and Appendix

The Government of Honduras and the Government of the United States of America have agreed as follows:

1. The Government of the United States will fully consult and coordinate with, and shall request appropriate authorization from, the Government of Honduras regarding the construction of new or improvement of existing Honduran military installations and sites which may be undertaken by the two Governments for their mutual interests. This engineering activity may be performed by United States Government personnel or contractors. As used in this Protocol, the term "contractors" includes subcontractors, and the Spanish term "instalaciones" means the same as the English term "installations and sites."

2. Permanent construction, including permanent structural improvements, must be approved in advance by appropriate Honduran authorities. Plans, specifications, and general project supervision will be coordinated with these authorities.

3. Removable or relocatable construction shall be undertaken only with the prior authorization of the Honduran commander of the installation or site where such construction is to be undertaken.

4. Honduras shall make available to the United States the use of land, easements, and rights-of way necessary for agreed-upon construction. When such property is owned by the Government of

Honduras, use shall be provided to the United States without cost; when such property is privately owned, the United States will compensate Honduras or the property owner concerned in an agreed manner and amount for costs incurred in obtaining use of the property in accordance with Honduran law.

5. For the construction, improvement, repair, or maintenance of Honduran installations and sites covered by this Protocol, and for the installation and maintenance of its equipment, the Government of the United States may, under applicable United States law, regulations, and procedures, utilize its own personnel or qualified contractors of its choice. To the maximum extent possible, available and qualified Honduran contractors will be utilized. Employment of Honduran and third country personnel by contractors will be in accordance with Honduran labor law.

6. The United States Government or its contractors shall retain title to all movable property brought into or purchased within Honduras for activities undertaken pursuant to this Protocol, unless title is transferred by the United States Government or its contractors to the Government of Honduras. Such property shall not be subject to Honduran duties, taxes, or other charges. When no longer used for purposes of the

Protocol, such property will be subject to Honduran duties, taxes, or other charges unless transferred to the Government of Honduras or exported.

7. For activities undertaken pursuant to this Protocol, United States contractors, and personnel employed by United States contractors who are not nationals of, nor ordinarily resident in, Honduras, shall not be subject to Honduran duties, taxes, or other charges.

8. The Government of Honduras will facilitate entry into, movement within, and exit from Honduras of United States 2 contractor personnel. Entry into Honduras by third country nationals employed by the United States Government or its contractors, in the absence of qualified Honduran personnel, shall be subject to applicable Honduran immigration regulations.

9. While in Honduras, United States Government and contractor personnel may possess and carry individual weapons when authorized to do so under procedures agreed to by competent Honduran authorities, following a request by United States authorities.

10. The United States Government and its contractors may utilize existing Honduran public services for construction, improvement, and use of installations or sites, provided such

use of public services does not significantly affect local consumers. These services will be provided at the most favorable rate at which such services are provided to Honduran Government agencies, but free of any tax or comparable fee, and shall be paid for by the United States Government or its contractors. When such services are not available, the United States Government may establish them.

11. Maximum practicable use shall be made of Honduran goods and services, consistent with United States laws and regulations, when purchases are made for the construction, improvement, or use of installations and sites in Honduras. For the purchase of goods and services for which prices are regulated by the Government of Honduras, the United States Government and its contractors shall be entitled to a price not to exceed that paid by the Honduran Armed Forces, but free of any tax or comparable fee.

12. Permanent structures erected on land owned by the Government of Honduras pursuant to this Protocol shall be owned by the Government of Honduras. The United States Government shall have the right to use any permanent structures which it has constructed or improved under the provisions of this Protocol.

13. Installations or sites shall be under Honduran command. United States Armed Forces using them shall be under United States command. The Honduran commander shall have access to all installations or sites. Access to cryptographic areas and classified equipment or information will be governed by mutually agreed procedures.

14. When installations or sites are used by United States Armed Forces, the United States Government shall contribute to the maintenance and repair of such installations or sites in proportion to their use by the United States Armed Forces. Appropriate United States and Honduran authorities will enter into technical arrangements which will establish appropriate factors for determining specific maintenance and repair responsibilities under this paragraph. [The Agreement between the Government of the United States of America and the Government of Honduras for maintenance and repair of Honduran Aerial Ports signed on May 20, 1985 will become an annex to this Protocol.]

15. An inventory listing characteristics and functions shall be kept for each of the installations and sites to which this Protocol applies. When the United States Government no longer requires use of a particular installation or site, it shall be

returned to the Government of Honduras. Any installation or site so returned will include its permanently-installed systems for providing power and water. While in the process of vacating installations or sites, the United States Armed Forces will endeavor not to damage them. The United States Government or its contractors may remove or otherwise dispose of their equipment or other movable property located at such installations or sites.

16. Due consideration will be given to the security interests of both Governments prior to the disposition of any equipment, materials, supplies, relocatable structures, or other movable property imported into or procured within Honduras under this Protocol which is deemed essential to the principal mission of an installation. The Government of Honduras shall have the first option to acquire, consistent with Honduran law, any such property which the United States Government, in accordance with United States law, may dispose of within Honduras.

17. Honduran authorities retain the right to approve the maximum level of United States Armed Forces in Honduras and to approve or reject any deployment of United States Armed Forces into Honduras. Prior to the execution of any approved deployment, the Government of Honduras shall be advised of: principal units to be deployed; the number and types of aircraft and ships and their principal activities; the number

of land vehicles and weapons systems; types of communications; and the number of United States military and civilian personnel. Appropriate Honduran authorities shall be duly informed regarding relief forces and reductions or increases in personnel, equipment, or material.

18. The Honduran commander of the installation or site at which United States Government personnel are located shall be informed of the types of equipment and material in the possession of such personnel.

19. Procedures for the storage and handling of United States weapons systems in Honduras shall be mutually agreed. The appropriate Honduran authorities shall be informed periodically of the amounts and types of munitions and weapons stored by United States Armed Forces on Honduran territory.

20. The Government of Honduras will be responsible for protecting installations and sites against any external threats. It will afford prompt access, in conformance with agreed security procedures, to the installations and sites by United States Government and contractor personnel. Responsibility for internal security at installations and sites will be agreed upon by the United States and Honduran Armed Forces.

21. Prior approval of the Government of Honduras will be required for entry into Honduras of aircraft and ships operated by or for the Government of the United States (hereinafter referred to an United States aircraft and ship). In this regard:

(a) Entry of United States aircraft and ships participating in exercises will be in accordance with arrangements established pursuant to Protocol II to the 1954 Military Assistance Agreement; and

(b) Entry of United States aircraft and ships providing routine support to United States forces will be approved on a monthly basis.

(c) Approval for the entry of other United States aircraft and ships not participating in exercises or maneuvers nor providing routine support will be requested 48 hours in advance, except in unusual or unforeseen circumstances.

Aerial Ports	Sea Ports
Goloson	Henecan (San Lorenzo) in the Pacific
Palmerola	Puerto Cortes in the Atlantic
Toncontin	

In the event that one of the named aerial ports is temporarily not available as a port of entry, an alternate port may be used.

b. United States aircraft and ships may use the foregoing ports, and additional ports as agreed by both Governments, for fueling or refueling, maintenance, supply, visitation, and other related activities. Such use will take into account the normal functions of these ports.

23. United States aircraft and ships shall be exempt from navigation charges, tolls, port charges, landing fees, and other charges which do not constitute compensation for services requested and received.

24. Operations of United States aircraft and ships in Honduran territory outside the Honduran air and maritime route structure will be in accordance with procedures agreed between

appropriate United States and Honduran authorities regarding special use of air space and territorial waters.

25. Honduras reaffirms its obligations under the Treaty for the Prohibition of Nuclear Weapons in Latin America, and the United States reaffirms its obligations under Additional Protocols I and II of that Treaty.

26. The authorities of the Government of the United States, acting within their legal compentence, will pay just and reasonable compensation in settlement of meritorious claims arising out of acts or omissions of members and civilian employees of United States Armed Forces done in the performance of official duty or out of any act, omission or occurrence for which the United States is legally responsible. The Government of the United States may also at its discretion settle meritorious claims not arising from the performance of official duty and for which it is not otherwise legally responsible, but in the absence of such settlement the injured party may seek recovery of his damages from the responsible member or employees in Honduran courts. All claims processed by the authorities of the Government of the United States will be settled expeditiously.

27. The United States will share with Honduras, in a useful and timely manner, agreed-upon benefits which may be derived

from United States activities or installations in Honduras. Arrangements to implement this provision will be developed between the parties.

28. Appropriate authorities of the Governments of Honduras and the United States shall agree upon those arrangements necessary to implement this Protocol.

29. The Governments of Honduras and the United States shall instruct their appropriate authorities to ensure that the obligations set forth in the Protocol and its implementing arrangements are fully implemented and observed.

30. This Protocol and its implementing arrangements may be amended by means of a written agreement between appropriate Honduran and United States authorities.

31. Disagreements which may arise concerning this Protocol or its implementing arrangements shall be resolved by appropriate Honduran and United States authorities.

32. This Protocol shall enter into force through an exchange of diplomatic notes confirming that both Governments have completed their respective internal procedures. It will remain in force for the duration of the Bilateral Military Assistance Agreement between the Governments of the United States and Honduras, signed May 20, 1954.

33. This Protocol will not apply to construction projects undertaken pursuant to United States Security Assistance programs or to construction-type activities undertaken within the context of military exercises conducted in accordance with Protocol II to the Bilateral Military Assistance Agreement of May 20, 1954 between the Governments of the United States and Honduras.

IN WITNESS WHEREOF, the undersigned, being duly authorized by their respective Governments, have signed this Protocol.

DONE at __________, this _______day of _______ 1987, in duplicate, in the Spanish and English languages, both texts being equally authentic.

FOR THE GOVERNMENT OF HONDURAS:	FOR THE GOVERNMENT OF THE UNITED STATES OF AMERICA:

FUNDING FOR NICARAGUAN REFUGEE REPATRIATION

Questions. How much money does the FY 91 A.I.D. budget provide for repatriating and resettling refugees and displaced persons in Central America? Do you anticipate that this amount will be adequate given the outcome of the Nicaraguan elections?

Answer. The Administration request for a supplemental fiscal year 1990 appropriation to assist Nicaragua contains $15 million to support the repatriation of a large number of the 60,000 Nicaraguans registered as official refugees in the region, mainly in Honduras and Costa Rica. It would also help some of the externally displaced and undocumented Nicaraguans in Central America, estimated at anywhere from 200,000–535,000 to return home and reintegrate. (The Administration request also contains funds for assistance to Nicaraguan Resistance returnees.)

When the Congress appropriates the $15 million, we anticipate contributing up to $10 million to the international repatriation funding appeals of the International Support and Verification Commission (CIAV), composed on the UN and OAS Secretaries General. The United Nations High Commissioner for Refugees (UNHCR) will be the implementing agency for UN/CIAV. We expect to use the other $5 million to support repatriation and reintegration programs and projects resulting from the International Conference on Central American Refugees (CIREFCA). Both these efforts will be important in furthering the ongoing Central American peace process which is so intricately connected with the repatriation, resettlement and reintegration of the Nicaraguan refugees.

Our funds will be contributed to international appeals and we expect that other donors will also be forthcoming. And, as refugees begin to return home, some resources used by international organizations to provide for their care and maintenance can be reprogrammed for their repatriation. If these expectations are borne out, sufficient funding should be available for initial repatriation efforts.

Question. Is there evidence that people are spontaneously returning to Nicaragua from exile in greater numbers as a result of the elections? Has the Chamorro government made any statements welcoming refugees back to Nicaragua? Do you expect that such a statement will be made after the inauguration?

Answer. We have been informed by the Office of the United Nations High Commissioner for Refugees (UNHCR) that since the February 25th elections in Nicaragua, some 1,000 Nicaraguans have returned to their country from Honduras, Costa Rica and Guatemala with UNHCR assistance. Almost 100 people have reportedly returned to Nicaragua in spontaneous repatriations since that time. UNHCR has also registered more than 1,100 people who have expressed a desire to repatriate after Mrs. Chamorro's government is in place.

The government-elect has not yet made any official statement but has indicated in correspondence the desire to have international organizations assist in the return and reintegration of Nicaraguans who have had to leave the country. Clearly, it is cognizant of the importance of repatriation issues and is discussing them with all concerned. We trust that after the inauguration, the positive attitudes of Mrs. Chamorro's government toward repatriation and reintegration will become increasingly apparent.

Question. If there is a large repatriation of refugees back to Nicaragua after the inauguration, what role do you anticipate the United States will play? Are we prepared to contribute to a large repatriation/resettlement program? Is it in U.S. interests to play a major role in such a program?

Answer. Based on the assumption that many Nicaraguans will want to repatriate to their country after Mrs. Chamorro's inauguration, the Administration is already preparing to play a major role in carrying out a structured and orderly international repatriation program.

Our pending request to the Congress for a supplemental fiscal year 1990 appropriation would provide $15 million for the purpose and, we expect, would stimulate other prospective donors to contribute to the program.

We fully support the Central American peace process which aims to end conflict and create democracy and stability throughout the region. A crucial component in achieving these goals is the solution of the area's refugee problem. We are determined that all concerned seize the opportunity presented by the developments in Nicaragua to further the process and significantly diminish the refugee problem.

We have a major and unique stake in the future of the Central American area and, especially in this instance, plan to play a role commensurate with our interests.

Question. If there is a large repatriation of refugees to Nicaragua after the inauguration, do you expect currently planned bilateral programs to provide for the refugees as well?

Answer. Yes. Currently planned repatriation programs will be part of a much broader commitment to Nicaraguan democracy, reconciliation and reconstruction. The President has announced a small immediate action program which can be carried out without new legislation. Such program will include funds for the repatriation of the Resistance and their families, and, for medical care under the Survival Assistance from Civilian Victims of Civil Strife in Central America Program ($7.5 million).

The FY 1990 Nicaraguan Supplemental seeks $300 million for assistance to include $47 million to be used, directly or through international organizations, to support the demobilization process and to reintegrate Resistance, displaced Nicaraguans and Nicaraguan refugees into the national social, economic, and political life.

We have underscored to the Nicaraguans that the moral obligation to the Resistance would be fulfilled by the U.S., and we have outlined the assistance package that will be utilized for resettlement in Nicaragua, which is designed to reestablish refugees and other Nicaraguans as productive members of their country.

Question. Given a change in the political direction of the Government of Nicaragua, what conditions would need to be created in Nicaragua to encourage Nicaraguans currently in the United States to return to Nicaragua? Is this group of refugees/economic migrants included in your planning for Nicaraguan assistance; for Central American bilateral programs in general?

Answer. We hope many Nicaraguans in this country will return to help rebuild Nicaragua's shattered economy in a new atmosphere of freedom. However, many of these people also have legal status in the U.S., including permanent resident status. Some of them may be reluctant to return to Nicaragua.

Those who fled the Sandinista regime did so primarily to find greater freedom and economic opportunity. Before they return to Nicaragua, they will likely want assurances of greater freedom and opportunity there. This means the Sandinistas must fulfill their promise to give up control over the state, including the Army and security forces.

President-elect Chamorro has promised to privatize inefficient state-run industries and rebuild Nicaragua's economy on free market principles. Her government needs help immediately for these tasks. The Sandinistas looted many government offices, left only $3 million in the treasury and gave President Chamorro an economy in ruins. Quick action on the Administration's proposal for $300 million in aid to Nicaragua this fiscal year and $200 million next year is vital to show U.S. support for the Chamorro government, to help rebuild the economy and to give exiled Nicaraguans confidence in a brighter future in their country.

The Administration proposal includes $15 million to repatriate and reintegrate Nicaraguan refugees into Nicaragua's social, economic and political life. These funds were requested for programs for the more than 300,000 Nicaraguan refugees in neighboring countries in the region, especially Honduras and Costa Rica. Quick economic improvement in Nicaragua itself will be the strongest factor in encouraging the return of Nicaraguans now in other countries, including the U.S.

NEW INTERIM GOVERNMENT IN HAITI

Question. On March 10, 1990, Lt. General Prosper Avril resigned as Haiti's president and head of the army. Avril had come to power through a coup 18 months earlier. Last January, he imposed a state of siege, and forced several leading opposition figures into exile. For the opposition this was a final indication that Avril could not be trusted to carry through with his stated commitment to elections. A political coalition, known as the Group of 12, pressed for Avril's resignation, which the general public had called for in nationwide protests. The Group of 12 chose Ertha Pascal-Trouillot, Haiti's only female Supreme Court judge, and a legal scholar, as interim president to oversee scheduled presidential and legislative elections this year. She will govern with a 19-member Council of State, which will have veto power over her, and will also be appointed by the 12 political groups.

What is the Administration's view of the interim government? Does the Administration plan to lift any of the sanctions that were imposed against the Haitian military governments? Has the interim government asked for any additional U.S. economic assistance? How does the Administration plan to support the democratic process in Haiti?

Answer. The Administration believes that President Trouillot genuinely is committed to free elections and supports her in this effort. As to "sanctions," that would be up to Congress which imposed conditions on assistance to Haiti following the 1987 election violence that have been continued in legislation since that time. The Trouillot Government has requested that the USG provide assistance to help stabilize the economic and political climate in Haiti and prepare for elections. Once legislative conditions governing assistance to Haiti have been met, the Administration, in consultation with the Congress, plans to provide appropriate assistance to the Trouillot Government on an incremental basis to enhance prospects for secure and credible elections. We will also work closely with other interested governments and the U.N. and OAS which have indicated a willngness to provide electoral assistance to Haiti.

Question. Haiti's attempt at democratic elections in November 1987 ended when at least 34 voters were killed at the polls. The army facilitated or contributed to the election violence. Do you believe conditions are different enough now to allow for a peaceful election process? Why or why not? What is the army's attitude toward democratic elections? What are the chances that Haiti will be able to hold free and fair elections this year?

Answer. At the time of the November 1987 election violence, the leadership of the Haitian Army was deeply suspicious of elections. Since that time, most of the senior leadership of the army has been changed. Current army commander, General Abraham, who has publicly pledged the army's support for the Trouillot Government and elections, has dismissed over 1000 officers, non-commissioned officers, and soldiers whose commitment to elections might have been questionable. Abraham and the army high command also backed President Trouillot's order to dismiss hundreds of "civilian attaches" to the army who had ties to the former military government and to hardline Duvalierist elements opposed to political reforms. We continue to be concerned about the prospects that hardline rejectionist elements may attempt to disrupt elections through violence as they did in 1987. In this regard, we believe it essential to provide the Trouillot Government and the Haitian Army appropriate assistance designed to help them thwart rejectionist efforts to block elections. With such assistance, we believe that there are realistic prospects for free and secure elections in Haiti this year.

Question. Most analysts believe the military aborted the 1987 elections because it feared the leading presidential candidates would try to reduce the military's power, and prosecute Duvalierists for human rights violations. In January 1988 Leslie Manigat won elections engineered by the army, but when Manigat tried to stand up to the military, he was overthrown and a military dictatorship was established. Do you believe the military is likely to accept the presidential candidates who will emerge in the upcoming elections? What constraints will the military still be able to impose on a civilian president?

Answer. Army Commander Abraham, who enjoys the confidence of President Trouillot and also that of Haiti's political leadership, has publicly pledged the army's support and loyalty to the Trouillot Government. Further, the army high command's dismissal of over 1000 army members and hundreds of "civilian attaches" to the army, all suspected of being anti-democratic elements, is an indication that it will fulfill its pledge of support to President Trouillot and elections.

Question. Chief of Staff General Herard Abraham now commands the Haitian army. Abraham reportedly has a "clean" reputation, and is not associated with the atrocities of past governments, but also lacks the broad support among the military that Avril had. How much control do you believe Abraham has over the Haitian military? Do you believe he will be able to restore discipline in the army and improve the army's human rights record?

Answer. Measuring the degree of control a Haitian Army Commander has over his forces is a subjective and difiicult proposition. However, I can say that Army Commander Abraham appears to enjoy the confidence of President Trouillot, Haitian political leaders, and the bulk of the officers and men of the Haitian Army. His recent dismissal of over 1,000 soldiers whose loyalty he thought questionable, and hundreds of "civilian attaches" to the army with close ties to the former military government and hardline Duvalierists, provides evidence that General Abraham is successfully establishing control and discipline within the Haitian Army. Abraham's most formidable immediate challenge in effectively controlling the Haitian Army is to find the means to address the legitimate demands of rank-and-file soldiers for improvements in their living conditions. Abraham's success in this regard—thereby also demonstrating that democratic reform was in the army's interest—would improve prospects of army support for the electoral process.

Question. Who are the leading contenders for the presidency in Haiti? What are their basic political platforms? How would U.S. interests be affected by their election? What is the military's attitude toward each of the chief contenders?

Answer. As yet, there are no reigstered candidates for elective office. While certain parties have designated their nominees, we do not wish to anticipate the process by singling out potential candidates or referring to their possible positions at this early stage. The U.S. Government supports a secure and credible democratic process in Haiti that leads to the free election of a civilian government. We have made it clear to all sectors of Haitian society that our goodwill is contingent on their support of democratic reform and respect for human rights. We do not now, nor will we in the future, support any particular candidate for any elective office in Haiti. We will support the efforts of the Trouillot Government, as well as that of other leading sectors of Haitian society, to bring about secure and credible elections. We are confident that we will be able to maintain a mutually beneficial relationship with any freely elected governemnt in Haiti. Conversely, the U.S. Government will not support, nor engage in a business-as-usual relationship, with any government in Haiti that comes to power through other than democratic processes.

SUBMITTED TO THE AGENCY FOR INTERNATIONAL DEVELOPMENT

ENVIRONMENTAL ACTIVITIES IN LATIN AMERICA

Question. In the FY 1990 Appropriations bill, A.I.D. is requried to increase the number of its environment personnel and devote increased attention to actions to counter global warming, including strategies in areas such as reforestation, end-use energy efficiency, least cost energy planning, renewable energy, etc.

Does the LAC Bureau possess sufficient numbers of environment specialists to carry out increased activity in this area in the Latin America region?

Answer. The Bureau for Latin America and the Caribbean (LAC) is actively seeking a way to use the authority given in the Fiscal Year 1990 Appropriations Bill to use program funds to hire additional experts. However, this new program funding authority ends on September 30, 1990, and if Congress does not extend it, these environmental experts would have to be transferred over to the extremely tight operating expense account or they would have to be let go. As a result of this potential problem, A.I.D. is being cautious in bringing on new staff. I am seeking to assure the adequacy of the LAC environmental staff.

Question. Do the missions receive sufficient support from the Science and Technology Bureau on environmental issues?

Answer. The LAC Bureau places a high value on the environmental assistance it receives from the Science and Technology Bureau, but that it is limited. The LAC Bureau relies principally on its own environmental office which has a good understanding of the specific issues in the region and a direct administrative relationship with the missions and senior policy makers in the Bureau.

Question. What is the current Latin America Bureau position on environment? Will it be a priority item on your agenda?

Answer. The LAC Bureau has taken a leadership role in integrating environmental considerations in development assistance programs, including the area of environmental protection. I would continue to stress the Bureau's leadership role in environmentally sound development and environmental protection.

Question. The International Development and Finance Act of 1989 authorizes A.I.D. to furnish assistance to NGOs for purchase of discounted commercial debts of foreign governments as part of a debt-for-nature exchange. Many believe Latin America is the region where this authority is most applicable. What is your view on debt-for-nature swaps? How do you intend to promote such exchanges?

Answer. Because of their relatively small size, debt-for-nature swaps will not have a major impact on the serious debt burdens afflicting Latin American countries, but I strongly support them for two reasons. First, they are a creative mechanism to bring more resources to bear on the critical issue of environmental and natural resource management, and second, they tangible demonstrate the participating country's willingness to search for solutions to their debt problems. I give my full support to efforts to develop debt-for-nature swaps.

PRIVATE ENTERPRISE ACTIVITIES IN LATIN AMERICA

Question. During the past decade, A.I.D./LAC has supported the privatization of government parastatals in several counties, including Costa Rica and Honduras. In your view, have privatizations supported by A.I.D. had positive results for Latin American economies?

Answer. A.I.D. has supported privatizations in several LAC countries. For example, A.I.D. missions in Honduras, Costa Rica and Jamaica have each initiated comprehensive programs aimed at privatization of a multiple number of state-owned enterprises (SOE).

Privatizations are designed to have positive effects on the economy. First and foremost are the anticipated improvements in efficiency inherent in the transfer of management form the government to the private sector. SOEs often require government subsidies to survive, and even when an SOE is profitable there is almost always room for more efficient production, cost savings and profit.

A good example of an A.I.D.-supported privatization program is in Honduras, where 14 out of 60 SOEs have been privatized and another 30 are in the final preparation stage. Most of the privatized companies have required substantial rehabilitation and new investment to reach the productivity goals of their new owners. Estimates of positive economic benefits in the 14 completed operations include:

New employment	2,500 jobs
New annual salary generation	US$ 6.9 million
New annual export generation	US$ 7.7 million
New annual fiscal revenues	US$ 3.6 million
New investment after privatization	US$9.4 million.

Other positive results of privatization include the opening up of sectors of the economy to competition through the elimination of state monopolies, reductions in government deficits through the elimination of the need to subsidize unprofitable SOEs, and the possibility of reducing the foreign debt through debt/equity swaps. For example, A.I.D. is currently providing a modest program of training assistance to the Government of Argentina's ambitious privatization efforts, several of which involve anticipated debt/equity swaps.

Question. Have they led to greater unemployment, as some critics predicted?

Answer. As seen from the Honduras example, privatizations tend to result in a net increase in employment as underutilized capital assets are reactivated and additional investments are made to bring the privatized company into efficient operation. The criticism that privatizations may lead to greater unemployment is more accurate in the case of SOE closures, which is not the same thing.

Question. Do you support a continued A.I.D. role in privatization?

Answer. Yes. In fact, in addition to the three LAC missions mentioned as having active privatization programs, there is great interest in pursuing similar efforts in El Salvador, Guatemala, the Dominican Republic and, recently, Panama and Nicaragua. I continue to support suh programs as part of an overall strategy to reduce the role of the state in the economy while promoting the private sector.

Question. A.I.D. has been active in microenterprise support activities for 10 years and since FY 1988 has been required under appropriations legislation to fund microenterprise projects (in FY 1988, $50 million; in FY 1989 and 1990, $75 million). Recently, the public interest lobbying group, RESULTS, has criticized A.I.D. for not properly implementing the microenterprise earmark. They claim that A.I.D. is not spending the money they claim to be spending on microenterprise and that the funds tend to go toward providing loans larger than the $300 or less recommended by the Congressional report, i.e., to more well-off entrepreneurs. Their examples come specifically from Central America. What steps do you plan to take to ensure that the Latin America missions implement the microenterprise credit earmark in accordance with Congressional requirements?

Answer. Microenterprise lending in the LAC region has expanded considerably under A.I.D. program in the last several years. A.I.D. has met the earmarks set out by the Congress for microenterprise lending, but has differed in its definition of what constitutes a microenterprise.

The report language associated with the microenterprise earmark identifies priority for loans in the range of $100 to $300, with a target population of the poorest 20% of the population in each country.

It is important to note that, in many countries in the LAC region, these absolute dollar amounts are very different in buying power than in other parts of the world. The Panamanian economy, for example, is extremely different from the economy in Bangladesh or, for that matter, from that in Nicaragua. The average hourly wage of those employed in Panama is $1.30 per hour, while in Nicaragua the average daily wage in rural areas is about $0.35. Because of this, I believe that lending targets need to be set in each country on a case-by-case basis. I think that it is more appropriate to define a microenterprise by the number of employees (e.g., never more than 10) or by the status of the owner in the operation (i.e., whether the owner is uniquely a manager or whether the owner works alongside other employees in carrying out the business).

Also, placing uper limits on microenterprise lending can be counterproductive to our goals of helping small businesses grow. An upper limit on the loan amount will quickly be reached as the enterprise borrows, achieves growth and then returns later to borrow larger amounts based on the new status of the enterprise. The amount of financing available to the microenterprise will quickly become limited, frequently with no alternatives available as the businesses reach a need for credit greater than the $300 limit envisioned in the report language.

An example of microenterprise lending success in the LAC region is the A.I.D.-funded ACCION program, implemented by ACCION in Cambridge, Massachusetts and its 37 affiliates in 12 Latin American countries. These organizations lend $2 million per month to microenterprises with the average loan being under $200. Loss rates on these loans are negligible. A.I.D. is presently working closely with ACCION to develop sustainable expansion for these programs.

Question. What priority do you give microenterprise support in the context of the broad picture of A.I.D. assistance to Latin America?

Answer. I remain committed to microenterprise support and microenterprise lending throughout the LAC region. I believe that a large portion of economic activity in the region takes place in microenterprises and that the bulk of employment in the region is in these enterprises. I am seeking solutions which are sustainable in the long-term and which will not only provide credit, but also provide possibilities for placing deposit and earning interest. As A.I.D. develops its private enterprise portfolio in each country, it is systematically including microenterprise development, and credit availability as a portion of its strategy.

Question. An October 1989 conference of small and micro extrepreneurs in El Salvador came to one major conclusion: "the small and microenterprise sector, notwithstanding its importance to the national economy, doesn't enjoy government support . . ." and "the prevailing economic model implemented by the government contains a series of measures which favor large enterprise and negatively affect the small and micro sector . . ." In view of the major role that A.I.D. plays in economic policy reform, do you believe that A.I.D. should take steps to ensure that microentrepreneurs receive equal treatment in government policy?

Answer. At the macroeconomic level, government policy does not discriminate against small and microenterprises. The government's comprehensive economic reform program emphasizes market-determined factors such as exchange rates, interest rates, pricing, and elimination of tariff and non-tariff barriers to trade; and a tightened monetary policy to keep the lid on inflation. These policies neither favor nor discriminate against large or small firms per se. However, in the short-term adjustment period, many enterprises, large and small alike, face higher costs due especially to higher prices for imported production inputs and to tight credit. In the longer run, however, enterprises will derive benefits from the increased demand spurred by a growing and more efficient economy.

At the financial-sector level, the Government of El Salvador's (GOES) policy has, in fact, favored microenterprises by directing that 2.5% of all banking credit should go to these enterprises at subsidized rates. Moreover, the GOES has established a special credit line (additional to the previously mentioned 2.5% minimum) funded with local currency made available under U.S. balance-of-payments assistance programs. However, the policy has not been as effective as hoped because of administrative difficulties, and credit under the small and microenterprise credit line was limited in 1989 as a result of tightened monetary policy.

A.I.D. can best serve small and microenterprises at the policy level by supporting the GOES in its reform of the financial sector. Because the nationalized banking system in El Salvador cannot adequately service the needs of the private sector, the GOES is moving toward privatization and liberalization of the banking system. As part of our dialogue with the GOES on the reform, we will encourage them to open a rediscount facility on a market rate basis to any registered financial institution, public or private, to permit increased participation of lenders and the more efficient credit delivery to more members of the small and microenterprise sector.

Question. Some critics have noted the A.I.D. microenterprise support in El Salvador goes strictly to an institution located in the war zones of that country and suggest that A.I.D. is only interested in targeting assistance to the poor when the political situation requires it. Do you believe that other areas of El Salvador should receive A.I.D. microenterprise credit support.

Answer. Before addressing microenterprise assistance generally, I must refute the suggestion that A.I.D. is only interested in targeting assistance to the poor when the political situation requires it. A.I.D. is concerned about the poor in El Salvador from developmental and humanitarian perspectives, attempting to broaden their participation in the country's economic as well as democratic development. The A.I.D. portfolio includes major projects in the areas of rural development, health, education, and family planning that target the poor directly. Projects aimed at investment and export promotion have as a primary objective employment generation and therefore also benefit the poor.

A.I.D. sees small and microenterprise development as an important vehicle for broadening participation of the poor in the economy. The A.I.D. dollar portfolio includes two projects for small and microenterprises: the $6 million Small and Microenterprise Development project that focuses on urban small business in San Salvador and the $283,000 Eastern Region Enterprise Development project. In addition, A.I.D. has jointly programmed with the Government of El Salvador the equivalent of approximately $40 million colones (approximately $8 million) in local currency made available under U.S. balance-of-payments assistance for a special Central Reserve Bank credit line for small and microenterprises.

I agree that assistance to microenterprise needs to be extended to other areas of the country. Expanding coverage means not only making more credit available, but developing and strengthening institutions to provide the credit. This year, A.I.D. will initiate a $10 million Microenterprise Development project. The project will focus on developing a new institution to channel credit to microenterprises, as well as on providing credit to local communities via village banks. While the project will not provide nationwide coverage, it will expand support to microenterprises well beyond areas currently being served.

POLICY REFORM IN LATIN AMERICA

Question. How would you assess A.I.D.'s efforts to promote policy reform in Latin America?

Answer. A.I.D. has put a great deal of effort into promoting policy reform, applying the major lesson learned by the international development community over the past several decades: that economic performance is closely correlated with sound macroeconomic policy. In some countries—most notably Costa Rica—government leaders were quick to recognize the importance of macroeconomic reforms and moved rapidly to implement them. Elsewhere, changes took longer; but we have seen progress to varying degrees in all A.I.D.-assisted countries, although some of them have had to live through the consequences of their policy mistakes before moving to correct them. I believe that A.I.D.'s persistence in pushing macroeconomic policy reforms has paid off. A.I.D. is now strengthening its efforts to promote sectoral policy reforms.

Question. In promoting policy reform, have we paid enough attention to programs to assist the poor who might be hurt by the price increases and unemployment that often accompany such reforms?

Answer. Economic policy reforms, which are bound to be painful to some groups in society, are essential for avoiding even greater pain over the long run. I intend to work for effective policy reforms that minimalize the duration of temporary negative effects and also to encourage programs to cushion the impact of those effects on the most vulnerable segments of the population.

There is always a tension between short-term and long-term costs and benefits, and the appropriate mix varies from country to country. Costa Rica's adjustment beginning in 1982 was carried out quickly, and the initial painful effects on the poor were soon reversed as the economy recovered. The labor-intensive growth policies being implemented in Costa Rica have reduced the open unemployment rate to less than 4%. Costa Rica also had the advantage of already having a strong set of safety-net measures to cushion the temporary impact of its policy reforms on the poor. In other countries, where existing safety nets are not present, A.I.D. seeks to work with the host government to find ways to target special, short-term assistance to the poor in ways that do not detract from long-term growth.

Question. In the past, we have offered ESF funding as a carrot to countries adopting politically difficult policy reforms. But in fiscal year 1990 both El Salvador and Honduras have suffered reductions in ESF funding, despite the election of new presidents—Alfredo Cristiani in El Salvador, and Rafael Callejas in Honduras—who are committed to carrying out the suggested policy reforms. Will these countries feel that the United States is providing inadequate assistance for policy reform at a crucial time when they are attempting to implement the politically difficult reforms? What can we do to deal with this dilemma?

Answer. I think all A.I.D.-assisted countries in the LAC region recognize that the amount of ESF resources available in FY 1990 is not as great as they had hoped, and that all LAC countries face the prospect of reduced ESF funding levels. They also understand our desire to support the new governments of Panama and Nicaragua. A.I.D. has been very supportive of the policy reform efforts in El Salvador and Honduras, and in addition to making its own ESF resources available, A.I.D. has been working closely with them to see how it might be able to help them improve their access to resources from the international financial institutions.

ASSISTANCE TO NICARAGUAN RESISTANCE

Question. Public Law 100-14, enacted in April 1989, authorized A.I.D. to provide a third phase of humanitarian assistance to the Nicaraguan Resistance, including support for voluntary reintegration and regional relocation. Further, the Central American presidents' peace plan of August 1989 called for establishment of a joint commission composed of the United Nations and Organization of American States to oversee the demobilization, repatriation and relocation of the Resistance. To date, the Resistance has remained intact. A.I.D. has provided vocational training and civic education courses to prepare Resistance members for returning to Nicaragua. What else has A.I.D. done to support the goal of repatriation and relocation?

Answer. The Administration, including A.I.D., has supported the Central American Peace process—including voluntary repatriation and reintegration.

A.I.D. has repeatedly reinforced that policy in dealing with the Resistance and National Opposition Union (UNO).

A.I.D. refused Resistance requests for assistance which would run counter to that policy.

A.I.D. conducted extensive training to prepare the Resistance for reintegration into civilian life and economy.

A.I.D. offered to help the International Support and Verification Commission (CIAV), which is comprised of the UN and OAS, get organized; A.I.D. offered to fund CIAV, as an inducement for them to take responsibility for repatriation and reintegration, before A.I.D.'s obligating authority expired February 28.

When the UN and OAS could not agree on a single CIAV organization, but agreed on split responsibilities, A.I.D. made separate grants to both organizations to help them get started on reintegration pending Congressional action on reintegration funding.

A.I.D. has offered CIAV/UN food, cash, medicines, materials and supplies to help them catch up with the demobilization and reintegration process, which was moving faster than UN/OAS were prepared for.

Question. During the third phase, it has been reported that the Resistance has periodically increased its troop strength in Nicaragua. While continuing to supply food, quartermaster gear, and other assistance to combatants remaining in Honduras, A.I.D. has also provided cash-for-food payments and food rations for those combatants returning to Nicaragua. Has A.I.D. adjusted its program to ensure that assistance levels in Honduras reflect any reductions in the numbers of Resistance members? Further, has A.I.D. declined to increase its assistance levels for the combatants in Nicaragua?

Answer. A.I.D. has adjusted the levels of humanitarian assistance in Honduras downward to reflect the reduced number of beneficiaries. The only assistance provided to the Resistance in Nicaragua has been cash-for-food; A.I.D. declined to increase that program to signal U.S. policy discouraging armed reinfiltration. The cash-for-food program remained at 3,500 beneficiaries—the level at the time of the Bipartisan Accord.

Question. During the three assistance phases, A.I.D. and its contractors have spent considerable funds to purchase equipment, medicines and supplies for the Resistance. These items are currently located at various sites in Honduras, including a field hospital and Resistance camp sites. How does A.I.D. propose to dispose of these items at the end of the assistance program and what meaasures, if any, will be taken to ensure that the Resistance does not sell items, especially those with a high dollar value?

Answer. A.I.D. has established a policy of using non-expendable property in A.I.D.'s and contractors' control to support reintegration into civilian life. The commodities were first offered to CIAV/UN and its contractors/intermediaries, which are managing the reintegration from Honduras where the bulk of the property is. Second, the property will be offered to other entities (CIAV/OAS, PVOs, GON) which are working on reintegration. Third, the property will be offered to the USAID missions in the region which are conducting humanitarian development. Finally, unwanted property will be sold and the proceeds returned to the U.S. Treasury. We have asked the Resistance in writing to exercise due diligence over non expendable property in their control to avoid personal gain and foster benefit to reintegrating comrades.

Question. The deputy director of the A.I.D. task force in Honduras recently pled guilty to charges of accepting bribes from a consultant hired to support the contractor responsible for providing medical assistance to the Resistance. Has A.I.D. identified the extent of wrongdoing and its impact on the assistance program?

Answer. The A.I.D. organization and staff were hurt and disgusted that an employee administering humanitarian aid would break the law for personal gain. The employee resigned from A.I.D. the same day he pleaded guilty to the felony charge. A.I.D. inspectors and auditors have investigated every aspect of this wrongdoing.

SUBMITTED TO DEPARTMENT OF DEFENSE

EL SALVADOR MILITARY ASSISTANCE

Question. Gen. Thurman, current head of U.S. Southern Command has recently testified before Congress that the 60,000 man El Salvadoran Army could not defeat the 5,000 FMLN military force.

Would you, Mr. Rowan, care to elaborate on Gen. Thurman's assessment of the situation.

If our aim is to encourage negotiations, and there is no military solution to this war, and since two of the main conduits for aid to the FMLN have been cut off recently (Panama and Nicaragua), why are we continuing with a high military aid level to El Salvador?

Answer. First, the aid pipeline from Nicaragua to the FMLN has not been cut off. We don't know if the Chamorro government is going to be able to control the military and to force a shutdown of covert Sandinista support for the FMLN. Second, neither Nicaragua nor Panama are originators of aid to the FMLN. Fidel Castro forced the guerrillas in El Salvador to form the FMLN and is still their primary supplier. We see no evidence that he is about to give up on them in the near future. Third, over the last four years the amount of assistance required by the Salvadrans so that lost or damaged equipment could be replaced and the force modernized has been estimated by our embassy to average $120—$130 million per year. The actual amount received during that time has averaged $80 million.

General Thurman stated that negotiations were necessary to end the war. He is correct. Our military assistance provides leverage to President Cristiani in negotiations with the FMLN.

Military preparedness leads to political power at the negotiating table. If we want the war to end, President Cristiani needs our best backing. President Cristiani has stated that conditions at this time would be regrettable.

A purely military victory has never been a policy goal of either the Salvadorans or of the United States. Our long-standing goal has been dialogue toward a negotiated solution of the conflict. Unconditioned assistance is a major factor in securing a negotiated solution.

EL SALVADOR MILITARY CORRUPTION

Question. What are the reenlistment rates within the Salvadoran military?

Answer. Although the question alleges that reenlistment is discouraged to build up pension fund assets, personnel figures over the past few years do not support that contention. Over the past few years, reenlistment rates have increased from around 12% to approximately 28-30%. Budgetary pressures preclude increasing reenlistment rates further, because reenlistees are paid considerably more than enlistees.

I would like to provide some basic information about the military Social Security Institute (IPSFA). This organization provides physical rehabilitation and job training for injured soldiers; funerals for soldiers and survivor benefits for their families, permanent disability entitlements, life insurance, retirement pensions, personal loans, and mortgages. The overall operation is supervised by a board of directors, subject to annual audits by the Central Bank and Salvadoran General Accounting Office. Active duty military and public security force members plus civilians employed by the Armed Forces become members of IPSFA upon entering service or employment.

Question. Has anyone questioned General Ponce or sought to investigate the operations of the military cooperative?

Answer. Colonel Ponce was elected by members to head the Board of Directors of the Military Cooperative.

The cooperative has legal authorization from the Legislative Assembly to import merchandise duty-free for sale to its members. Merchandise is not sold at a profit, and is not sold on the open market.

A.I.D. STUDY ON AGRICULTURE IN THE CARIBBEAN BASIN

Mr. OBEY. At this point we will include in the record the Agency for International Development's report "Feasibility Study on the Potential Benefits of Joint Agricultural Research and Education in the Caribbean Basin Region" requested in the fiscal year 1990 report.

[The information follows:]

AGENCY FOR INTERNATIONAL DEVELOPMENT
WASHINGTON D C 20523

ASSISTANT
ADMINISTRATOR

JUN 08 1990

The Honorable David R. Obey
Chairman
Subcommittee on Foreign Operations
Committee on Appropriations
House of Representatives
Washington, D.C. 20515

Dear Mr. Chairman:

Pursuant to Conference Report 101-344, dated November 11, 1989, I am pleased to transmit the enclosed report "Feasibility Study on the Potential Benefits of Joint Agricultural Research and Education in the Caribbean Basin Region."

We appreciate the Committee's interest in examining common agricultural problems facing Caribbean Basin and U.S. producers of tropical horticultural crops. We found the assignment challenging and revealing, and trust that the study meets with the Committee's expectations.

Please let me know when this office can be of further assistance.

Sincerely,

R. Ray Randlett
Assistant Administrator
for Legislative Affairs

FEASIBILITY STUDY ON THE POTENTIAL BENEFITS OF JOINT AGRICULTURAL RESEARCH AND EDUCATION IN THE CARIBBEAN BASIN REGION

A REPORT TO THE 101st CONGRESS OF THE UNITED STATES

May 1, 1990

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LIST OF ACRONYMS

ADF	Agricultural Development Foundation (Dominican Republic)
AID	Agency for International Development
APHIS	Animal and Plant Health Inspection Service
AREP	Agricultural Research and Extension Project (of RDO/C)
CAAP	Private Agricultural Agroindustrial Council
CAEP	Caribbean Agricultural Extension Project (of RDO/C)
CARDI	Caribbean Agricultural Research and Development Institute
CARIRI	Caribbean Industrial Research Institute
CATCO	Caribbean Agricultural Trading Company
CATIE	Tropical Agricultural Research and Training Center
CBAG	Caribbean Basin Advisory Group
CBI	Caribbean Basin Initiative
CDB	Caribbean Development Bank
CSRS	Cooperative State Research Service (of USDA)
CTA	Center for Tropical Agriculture (in IFAS)
EAP	Pan American Agricultural School (Zamorano)
EARTH	Agricultural School for the Humid Tropics
FAMU	Florida A&M University
FAO	Food and Agriculture Organization of the United Nations
FHIA	Honduran Agricultural Research Foundation
FRED	Food and Resource Economics Department (in IFAS)
FPX	Federación de Asociaciones de Productores y Exportadores Agropecuarios y Agroindustriales de Honduras (formerly, FEPROEXAAH) (Honduras)
FUSADES	El Salvadoran Economic and Social Development Foundation
GDP	Gross domestic product
Gremial	Guild of Non-traditional Product Exporters (Guatemala)
IADB	Inter-American Development Bank
ICAITI	Instituto Centroamericano de Investigación y Tecnologia Industrial (Guatemala)
ICTA	Instituto de Ciencia y Technologia Agricola
IFAS	Institute of Food and Agricultural Sciences (at UF)
IPM	Integrated pest management
IICA	Inter-American Institute for Cooperation on Agriculture
ISA	Superior Institute of Agriculture (Dominican Republic)
JADF	Jamaica Agricultural Development Foundation
JAREF	Joint Agricultural Research and Education Feasibility Study
LSU	Louisiana State University
MOA	Ministry of Agriculture or its equivalent
NGO	Non-government organization
NTAE	Non-traditional agricultural export
OECS	Organization of East Caribbean States
PROEXAG	Non-traditional Agricultural Export Support Project
R&D	Research and Development
RDO/C	A.I.D. Regional Development Office for the Caribbean

REAC	Research and Education Advisory Council
ROCAP	U.S.A.I.D. Regional Office for Central America and Panama
TAMU	Texas A&M University
TARS	Tropical Agricultural Research Station
TREC	Tropical Research and Education Center
TROPRO	West Indies Tropical Produce Support Project
UF	University of Florida
UPR	University of Puerto Rico
USAID	United States Agency for International Development
USDA	United States Department of Agriculture
UVI	University of the Virgin Islands
UWI	University of the West Indies
WB	World Bank
WINBAN	Windward Islands Banana Producers Association

EXECUTIVE SUMMARY

The purpose of this study, as requested of A.I.D. by the 101st Congress of the United States, is to assess the feasibility and potential benefits of joint research and education on common problems facing agricultural producers in the Caribbean Basin, including producers in Central America, the Caribbean, and U.S. states abutting the Gulf of Mexico. The report focuses on common problems facing growers of tropical fruits, vegetables, and ornamentals.

A. Principal Findings

The study found specific problems common to Caribbean Basin and U.S. producers in states abutting the Gulf of Mexico. The most critical common problems are plant protection, including pesticide residues within tolerances; postharvest handling; and production constraints. Other problems common to horticultural producers, while less problematic to U.S. producers, are crop selection, transportation, market penetration (especially market intelligence, market linkage, quality control), and food processing technology.

The study found that research on and technology development and marketing for horticultural crops in the Caribbean Basin region are primarily carried out by the private sector as part of specific export commodity systems and organizations. In Central America and the Caribbean, public sector research and education institutions largely have focused on traditional export (banana, coffee, cacao) and food crops (grains), although some of these institutions are now developing research programs in support of development of non-traditional agricultural exports (NTAE) crops. But this research often is not coordinated or closely linked to grower needs, indicating a significant limitation in the technology development and transfer system for horticultural crops intended for NTAE markets. In the United States, public institutions are engaged in research on horticultural crops but relatively little of this research is carried out collaboratively or jointly with Central American or Caribbean researchers.

Although many production and marketing factors limit horticultural crop development in the Caribbean Basin region, the findings of this study strongly suggest that research and education efforts should focus on plant protection, postharvest handling technology, and production constraints. While there are differences between Caribbean Basin and U.S. producers of horticultural crops, all production and marketing participants share a concern in overcoming the problems identified. Cooperation through joint research and education could facilitate the development and transfer of technology that producers and other market participants require to enter and compete effectively in the marketplace.

B. Major Conclusions

There is a need for improved links and communication between technology developers, suppliers, and users to facilitate research on problem areas of common concern. This could be stimulated by a mechanism that (1) ensures systematic dialogue between public and private research and educational institutions; (2) strengthens the role of the private sector in establishing research priorities and in providing funding support for research; and (3) directly participates in technology transfer to producers through education, extension, and other means as appropriate.

The study evaluates four options for establishing a mechanism to address this identified need: (A) a new research and education center; (B) a new organizational unit within an existing research and education center; (C) strengthening research and education programs of existing research and education institutions; and (D) establishing a joint research and education program coordinated by a private international horticultural industry group. Each option was evaluated in terms of four criteria (staffing, coordination, likely impact, and cost).

Generally, significant limitations were found to be associated with establishing a new research and education center (option A) or a new organizational unit within an existing research and education center (option B). Option C provides a model of how donors might play a more active role in strengthening research and education programs of existing research and education institutions. In this model, however, the private sector's role is largely advisory, with the private sector having little, if any, direct control over how scarce research funds would be allocated. By comparison, option D provides for research funding to be channelled through a research and education program coordinated by a private international horticultural industry group. In so doing, option D provides a strong link between technology users in the private sector and researchers in the public and private sectors. This option also will serve to coordinate and strengthen research and education programs of public sector regional institutions.

Option D would provide, at least in the short run, an effective and efficient mechanism for getting agricultural researchers to focus more directly on the common problems that are of greatest concern to Caribbean Basin and U.S. horticultural crop producers. However, in the long run, the progress in technology development and transfer achieved through option D could be enhanced to the extent that the public sector research and education institutions participating in the program would be part of an overall horticultural research and education network such as that outlined in option C.

SECTION I

INTRODUCTION

A. Purpose of Study

The purpose of the study, as requested of A.I.D. by the 101st Congress of the United States, is to assess the feasibility and potential benefits of joint research and education on common problems facing agricultural producers in the Caribbean Basin, including producers in Central America, the Caribbean, and U.S. states abutting the Gulf of Mexico. The report focuses on common problems facing growers of tropical fruits, vegetables, and ornamentals.

B. Background

The 101st Congress, in the FY 1990 Appropriation bill, noted that agricultural producers in the Caribbean region, including Caribbean Basin Initiative (CBI) countries and the U.S. states abutting the Gulf of Mexico, have common prospects and problems. The Congress noted the following as potential common problems: proper crop selection and management, pest management, postharvest handling and treatment, transportation, and market penetration. Further, the Congress cited, as an example of a common problem, the declining research on and availability of environmentally safe pesticides and pest management technologies. The Congress expressed the view that it would benefit Caribbean and U.S. agricultural interests to seek solutions to common problems jointly.

The Congress directed the Agency for International Development (A.I.D.) to study the feasibility and the potential benefits to U.S. agricultural production and the objectives of the CBI of joint research and education on agricultural problems common to agricultural producers throughout the Caribbean Basin region. Responding to this requirement, A.I.D. mounted the Joint Agricultural Research and Education Feasibility (JAREF) study. For the interested reader, more detailed technical information about the study can be found in the JAREF Technical Report and annexes (153 pages), on file with A.I.D.'s LAC/DR/RD office. Table 1 list the annexes to this report.

The term "joint research and education," while not defined by Congress, is understood as meaning that U.S. researchers (or educators) collaborate with colleagues in Central American and Caribbean research and education institutions to develop agricultural research and/or education programs on problems common to Caribbean Basin producers. The study, according to the scope of work, assesses the role of public research and education in technology development and transfer for horticultural crops

Table 1. Annexes Available From A.I.D.'S LAC/DR/RD

Annex 1	Congressional Requirement for JAREF Study
Annex 2	Study Methodology
Annex 3	Profile of NTAE Production in Each Sub-Region
Annex 4	Other Common Problem Areas and Potential Benefits of Joint Research and Education 1. Crop Selection 2. Transportation 3. Market Penetration 4. Food Processing Technology 5. Technology Transfer 6. Organizational and Policy Constraints
Annex 5	Major Diseases of Tropical Fruits
Annex 6	A Partial Listing of Pests Attacking a Number of Commonly Grown Fruits in the Caribbean Basin Region
Annex 7	Principal Research Mandate of Research and Education Institutions Visited and/or Reviewed
Annex 8	Common Problems and Institutional Responses to NTAE Crops by Caribbean, Central American, and U.S. Southeast Research and Education Institutions
Annex 9	Major Problems in Agricultural Research and Education in the Caribbean Basin Countries
Annex 10	Economic Returns to Research and Education on NTAE Crops
Annex 11	Potential Contributions to Caribbean Basin Initiative (CBI) Objectives and U.S. Agricultural Production
Annex 12	Sustainability of Joint Research and Education
Annex 13	Site Visits and Key Informants Interviewed
Annex 14	Key Informants Interviewed by Telephone
Annex 15	Key Informants Who Replied by Letter
Annex 16	Key Informants Who Replied by FAX

(see subsection B.3. below), but the private sector finances and/or conducts a substantial portion of horticultural research in the Caribbean Basin region. However, the limited time and resources available to conduct this study precluded a full assessment of private sector agricultural research and education underway in the region.

1. Caribbean Basin Region: Geographic Overview

The Caribbean Basin region is defined as including:

- Central American countries: Belize, Costa Rica, El Salvador, Guatemala, Honduras, Nicaragua, and Panama;
- Caribbean countries: Aruba, Bahamas, Barbados, British Virgin Islands, Dominican Republic, Haiti, Jamaica, Netherlands Antilles, Trinidad and Tobago, and Eastern Caribbean states (Antigua and Barbuda, Dominica, Grenada, Montserrat, St. Christopher-Nevis, St. Lucia, and St. Vincent and the Grenadines); and
- U.S. states abutting the Gulf of Mexico: Alabama, Florida, Louisiana, Mississippi, and Texas. Although not U.S. states, Puerto Rico and the U.S. Virgin Islands also are included.

These countries are identified in the map on page 8, which also shows the acronyms of the key research, education, and export development organizations in the Caribbean Basin region and of major A.I.D.-assisted projects and institutions working on development of non-traditional agricultural export (NTAE) crops in the region. A brief description of these various organizations and projects is provided in the appendix of this report.

2. CBI Objectives

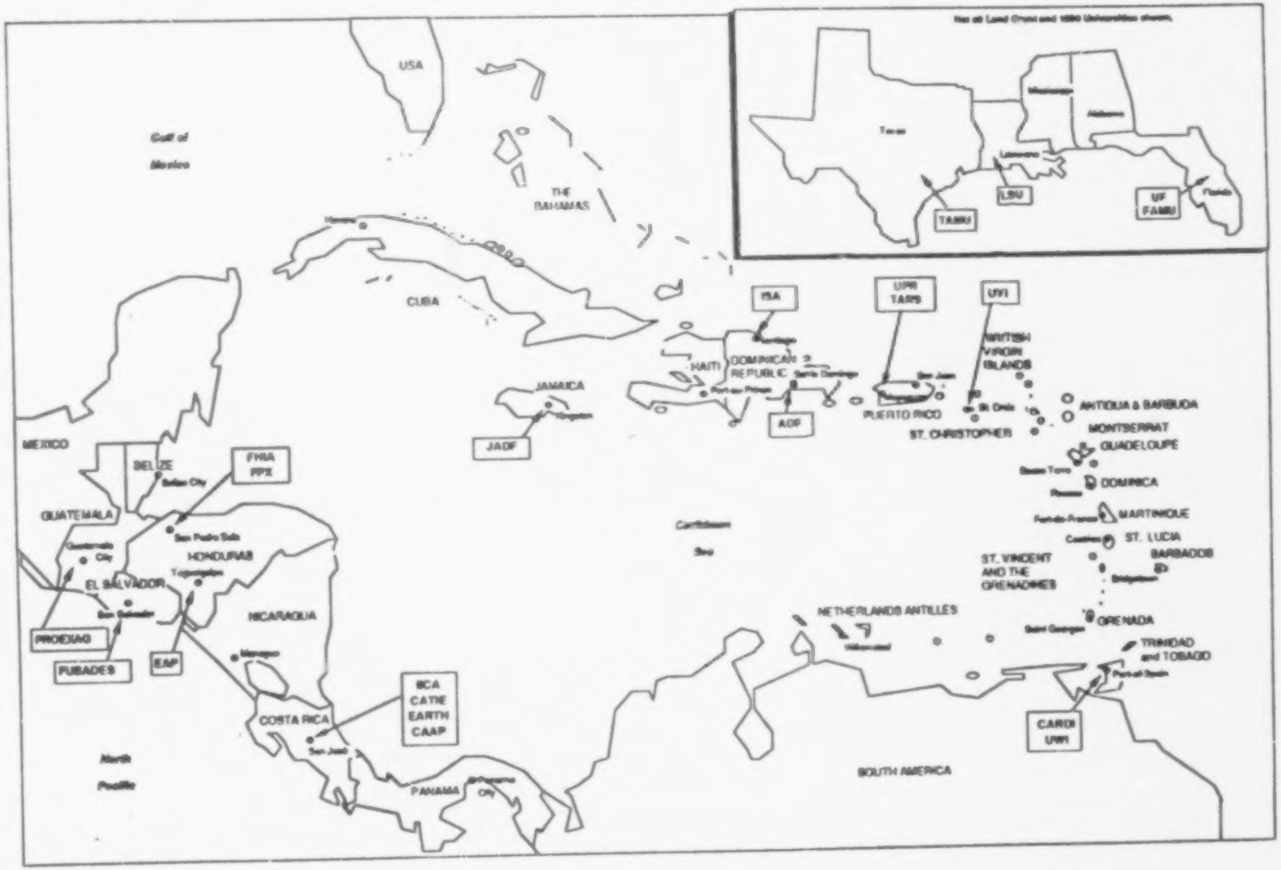
The objective of CBI is to promote economic development through private sector initiative in Central America and the Caribbean. The goal is to expand foreign and domestic investment in non-traditional sectors, diversifying CBI country economies and expanding their exports. Herein, the term "Caribbean Basin" refers in a general way to the Caribbean and Central American countries participating in the CBI program, while the term U.S. Southeast refers to the U.S. states abutting the Gulf of Mexico.

3. Rationale for Focus on Horticultural Crops

A variety of agricultural commodities are produced in the Caribbean Basin region; they include livestock, food and fiber crops (exclusive of horticultural crops), and horticultural crops, including fruits, vegetables, and ornamentals. With the economic opportunities (e.g., foreign exchange) created in the

Central American and the Caribbean countries by CBI, A.I.D. has placed increasing emphasis on horticultural crops with export potential. Accordingly, this study focused on the potential benefits of joint research and education on common problems facing Caribbean Basin and U.S. producers of horticultural crops.

Research, Education, and Export Development Organizations in the Caribbean Basin Region


Not all Land Grant and 1890 Universities shown.
Texas
Louisiana
Mississippi
Alabama
Florida
TAMU
LSU
UF
FAMU
USA
Gulf of
Mexico
THE
BAHAMAS
Havana
CUBA
JAMAICA
Kingston
JADF
HAITI
Port-au-Prince
DOMINICAN
REPUBLIC
Santiago
Santo Domingo
ISA
ADF
PUERTO RICO
San Juan
UPR
TARS
UVI
BRITISH
VIRGIN
ISLANDS
St. Croix
ST. CHRISTOPHER
ANTIGUA & BARBUDA
MONTSERRAT
GUADELOUPE
Basse Terre
DOMINICA
Roseau
MARTINIQUE
Fort-de-France
ST. LUCIA
Castries
BARBADOS
Bridgetown
ST. VINCENT
AND THE
GRENADINES
GRENADA
Saint George
TRINIDAD
and TOBAGO
Port-of-Spain
CARDI
UWI
NETHERLANDS ANTILLES
Willemstad
Caribbean
Sea
SOUTH AMERICA
MEXICO
BELIZE
Belize City
GUATEMALA
Guatemala
City
EL SALVADOR
San Salvador
HONDURAS
San Pedro Sula
Tegucigalpa
FHIA
FPX
PROEXAG
FUSADES
EAP
NICARAGUA
Managua
COSTA RICA
San José
IICA
CATIE
EARTH
CAAP
PANAMA
Panama
City
North
Pacific

SECTION II

OVERVIEW OF CARIBBEAN BASIN HORTICULTURAL PRODUCERS

A. Comparison of CBI and U.S. Horticultural Producers

Many farmers in the Caribbean Basin region are actively involved in producing horticultural crops. However, the total volume of horticultural crops that they supply to the U.S. market comprises only a small percentage of the total horticultural crops marketed in the United States. In recent years, Central American and Caribbean horticultural growers have shifted toward production of horticultural crops to meet growing market demand for these commodities in the United States and elsewhere. This trend implies a need throughout the region for additional research and education on how to grow and market these crops most efficiently.

The study found major differences in the three Basin sub-regions (Caribbean, Central America, and the U.S. Southeast) in the production and marketing environments faced by horticultural crop producers. Generally, horticultural producers in the CBI countries, relative to horticultural producers in the U.S. Southeast, face a less favorable production and marketing environment with respect to access to improvements in cropping technology and management systems, postharvest handling and processing technologies; and credit and agricultural inputs, transportation, markets, and research and extension.

With respect to agroclimatic conditions, the land tilled by U.S. farmers in the states abutting the Gulf of Mexico, with a few exceptions, is located within a temperate climatic zone in which crops can be grown only during the spring, summer, and fall months. However, the southernmost parts of both Florida and Texas have sub-tropical climates, with very infrequent freezing weather. These areas can grow many tropical crops that cannot thrive elsewhere in the continental United States. The lands cultivated by farmers in the CBI countries are in a tropical climatic zone in which crops can be grown the year round. This places CBI producers in an advantageous position to supply horticultural produce to the United States during those times of the year when U.S. farmers are not able to produce certain crops or to grow sufficient supply to meet market demand.

However, for various reasons including agroclimatic differences, producers in CBI countries cannot simply adopt U.S. horticultural production systems. These systems must be developed or adapted to fit the specific agroclimatic niches of each production plot. Thus, the farmer cannot use the same technology to grow the same crop on all plots. Hence horticultural growers in CBI countries need to adapt production technologies to the resource mix of each plot, thereby increasing the complexity of the management systems required to support production.

With respect to access to public/private research and extension, horticultural producers in the U.S. Southeast are served by a well-developed agricultural research, extension, and education system (Land Grant universities and other educational institutions). Farmers are well educated and have ready access to agricultural information sources through a variety of media, including contacts with research scientists in the university and USDA research systems. Further, agricultural extension agents, backed up by subject matter specialists, are assigned to each district. Finally, private firms that sell inputs or equipment to or buy produce from farmers have a vested interest in ensuring that farmers have the information needed to be able to grow top quality produce profitably.

By comparison, public and private sector sources of agricultural information are much less developed in the CBI countries. In many of these countries, research and extension budgets often are barely sufficient to cover salaries, with little left for research and extension expenses. Public sector research and extension tend to focus on traditional subsistence food crops and not on horticultural crops. Only farmers and entrepreneurs having sufficient resources to establish connections with U.S.-based information sources (e.g., U.S. universities, importers of horticultural crops, or private consultants) or with private sector companies in CBI countries can obtain the basic technology and inputs required to establish adaptive research and commercial production and exporting programs.

B. Common Problems Facing Horticultural Producers

Despite the differences between horticultural producers in the CBI countries and the U.S. Southeast, all horticultural producers, including farmers, growers, packers, processors, shippers, transporters, and importers, share a common concern in terms of overcoming problems that constrain efficient production and marketing of their crops in an increasingly competitive and interdependent global economy. This concern is most critical where producers face problems common to all three Caribbean Basin sub-regions.

The essential prerequisite for a successful horticultural enterprise is the ability to provide the market with a consistent supply of high quality products over an extended time. Meeting this prerequisite is a challenge facing all horticultural growers throughout the Caribbean Basin region. Insufficient product quantity or quality may be due to a number of problems commonly found in many Caribbean Basin countries.

Based on document reviews, site visit observations, and discussions with key informants, nine potential common problems were identified as follows: crop selection, production constraints, plant protection, harvesting/postharvest handling and management, transportation, market penetration, food processing technology, technology transfer, and organizational and policy constraints.

These problems were ranked in terms of three factors: (1) the immediate economic impact of the problem in the region (e.g., opportunity to earn foreign exchange); (2) the urgency of the problem (e.g., potential for environmental damage); and (3) the existence of a minimum institutional base for conducting technology development and transfer on the problem. Based on this ranking, described in detail in annex 4, three priority common problems were identified.

1. Plant protection,
2. Harvesting/postharvest technology and management, and
3. Production constraints.

These problems were found to place the most immediate constraints on successful horticultural industry development throughout the Caribbean Basin region, including U.S. states abutting the Gulf of Mexico. A basic theme underlies them, namely, that while the market demands a consistent supply of quality products, this goal cannot be attained without adequate use of postharvest technology in combination with plant protection and appropriate production technology.

Each common problem is now reviewed, with the order of presentation--plant protection, harvesting/postharvest technology and management, and production constraints--being a general order of importance of these common problems across all three subregions of the Caribbean Basin. At the same time, it should be noted (1) that not all horticultural producers place equal importance on any given common problem, and (2) that producers in the region also share concerns about other problems.

1. Plant Protection

CBI and U.S. horticultural crop producers face a major problem with respect to pest and disease management. Cultivars resistant to pests and diseases may be available for some crops, but in most cases the use of chemical pesticides currently is the only way to achieve economic control. Growers must apply pesticides at dosages sufficient to control pests, but not so high as to leave residues that exceed the tolerances of importing countries. The absence of pesticide registration for many horticultural crops limits pest management practices.

There is almost a total dependence on chemicals for pest and disease control, because of the availability and success of chemicals in crop protection. There is also a general lack of awareness of alternative control strategies for particular pest situations. Even when such alternative strategies are known, they have not been widely implemented. Biological control is not a system that can be adopted readily by small-scale farmers. Integrated pest management (IPM) combines a variety of control techniques to reduce/keep pest populations to acceptable levels. Pesticides are used only when the pest population reaches an infestation level at which the economic loss of not applying the required control would be greater than the cost of applying the control. Crops must be monitored regularly for pests and pest damage. IPM can provide an environmentally sound, cost-effective approach to control a wide variety of pests in a large number of crops, but lack of data in many areas of IPM limits the application of this tool in the Caribbean Basin region.

Most estimates of perishable crop production losses attributable to pests average from 25 to 35 percent, although precise data are not currently available. Postharvest losses of perishables from insects and diseases have been estimated to be 40 percent or more in CBI countries. It has been estimated that pests and diseases in Dominica cause a 50 percent loss in fresh fruits and vegetables. In addition, one must consider the cost of control practices, limitations or rejections of exports, the adverse impact on human health from pesticide poisoning, and inherent environmental contamination problems.

Because of insufficient research and extension, over-application of pesticides is a common problem. Also, excessive pesticide application can lead to development of resistance to pesticides in the pest to be controlled and the acquisition of pest status by previously harmless species (e.g., whitefly).

Tropical insect fauna are poorly known, and in some cases basic taxonomic studies simply have not been done. There is also the problem of where and to whom to turn for help in identification. A tropical insect taxonomic and identification center is urgently needed in the Caribbean Basin region.

A very serious problem for Caribbean Basin producers is the difficulty of obtaining the latest pesticide registration and tolerance information for horticultural crops, in order to satisfy EPA and FDA import requirements. Growers have suffered considerable losses because of loads rejected at the port of entry into the United States owing to illegal chemical usage or residue levels exceeding tolerance. In most cases, this is due to a lack of knowledge of the latest U.S. pesticide laws. U.S. producers also are concerned as they seek alternate pest management technologies to replace pesticides which are now or may become banned.

2. Harvesting/Postharvest Technology and Management

Success in any horticultural production and marketing operation is determined, to a significant extent, by postharvest handling; that is, by how the crop is handled (packed, stored, shipped, etc.) between the time that it is harvested and the time that it is sold to the consumer. However, little effort has been directed at improving postharvest handling systems in the CBI countries. U.S. horticultural producers also need improved postharvest handling technology to ensure their crops meet the requirements of destination markets within the U.S. and internationally. For example, the technology for handling mixed loads of fresh fruits and vegetables to small island states needs to be improved. The need for improved postharvest handling technology and management of horticultural crops is even greater in the CBI countries.

Correct harvesting techniques are directly related to market requirements. Major losses have occurred as the result of inappropriate harvesting procedures. The most serious problems are related to improper harvesting and field selection, improper packing schedules relative to market conditions, lack of knowledge of broker standards, and inadequate mechanisms for quality-control checks and feedback.

Producers, handlers, and consumers all place high importance on loss reduction, food quality (including safety aspects), and freshness of horticultural crops. Yet understanding the underlying biology of these crops is essential to developing and applying new or improved technologies in all aspects of handling, storage, and distribution of fresh horticultural commodities. Such commodities are composed of living, metabolizing tissues having a variety of characteristics, including their capacity to withstand the stresses of time, temperature, physical handling, and transport; to resist infection and/or spoilage by decaying organisms; and to develop and maintain quality. These characteristics constitute the basis for determining the requirements for successful storage, handling, and distribution.

All the care taken in producing a crop may be lost through poor postharvest handling practices. Horticultural crops are usually very perishable and even a few hours of postharvest mismanagement can significantly lower the quality and marketability of the commodity. Common problems facing growers of horticultural crops include inadequate precooling to remove field heat, lack of organization in grading and packing, use of improper packaging materials that are not designed to provide adequate ventilation or protect the contents against bruising during transit, improper storage temperature and humidity management, and incompatibility of mixed load storage. Postharvest technology is probably the universal weak link in the chain from production to consumption of horticultural crops.

The "brick and mortar" approach consisting of infrastructure investments such as cooling facilities, storage rooms, packing houses, and other related equipment is often underutilized or misused because of inadequate management capability. It is common to see vehicles waiting to be unloaded at the packing house in 35°C heat because of poor logistic and time control procedures or storage of commodities in a variety of incompatible cooling facilities.

Advancements have taken place in postharvest infrastructure in the CBI countries (e.g., pineapples in the Dominican Republic, melons in Central America, and bananas in the Windward Islands). But in general, postharvest systems have not been designed for specific crop needs and required equipment is often unavailable. Existing infrastructure, including marketing board facilities, and internal buying depots, is underutilized and cooling facilities for extra-regional shipping are lacking.

The lack of cooling facilities also has intensified losses related to unreliable air transportation. Highly perishable products often arrive at the airport with high pulp temperature, and any delays in air transit permit further deterioration. In recent years private companies have increased cooling and freezing facilities, particularly in Central America. In the Eastern Caribbean, there is a lack of refrigerated storage for fruits or vegetables, usually at both producing and receiving points. Common problems are the location, adaptability, and utilization of the infrastructure in order to maximize returns on investment. The management of these facilities is often the most difficult problem to overcome. A problem in several countries visited was the poor management and organization of packinghouse facilities.

3. Production Constraints

Beyond the specific problem of plant protection (discussed above), Caribbean Basin horticultural producers also face common production constraints of various types. For example, citrus and mango trees are subject to serious decline problems just as they reach production age in both the Caribbean and the U.S. Gulf Coast states. Studies of the problem in the United States repeatedly have been confounded by cold damage due to recurring freezes. This problem would be eliminated or reduced if some of this research were carried out in a warmer zone of the Caribbean Basin region.

Another serious problem in increasing fruit production is the availability of reliable, disease-free sources of budwood and rootstock seed. Mistakes made early in a tree's life cannot be reversed, and sound propagation material is the basis for successful production and marketing. Genetic advances with different varieties that are more resistant to pests and diseases and that facilitate biological control of such problems are of major concern to CBI and U.S. producers, particularly in Florida. All Caribbean Basin producers want varieties that have higher tolerances and resistance to pests and diseases.

Another problem faced by CBI and U.S. producers is that of acquiring crop production technology to support diversification away from traditional monocropping systems. While fruit and vegetable varieties have a theoretical yield potential controlled by the genes of the plant, rarely is this yield achieved because of climate, soil, and cultural factors that affect plant growth and productivity.

Many Caribbean Basin producers have relatively poor land available for planting. Soils may be low in fertility and have poor structure, poor drainage, and/or excess salinity. In Central American and Caribbean countries, fields often are too hilly for continuous row culture. Nearly all areas where horticultural crops are grown have periods of inadequate or excess precipitation, and irrigation and/or drainage control is needed to avoid yield reductions and adverse effects on crop quality. Tile and ditch systems can help minimize the effects of excessive rain. Raised beds can alleviate waterlogging.

A common problem among vegetable growers is whether to use hybrid seed or open-pollinated seed. Hybrid seed, much more expensive than open-pollinated seed, may offer advantages in terms of increased earliness, resistance to stress, and uniformity of product. However, production inputs need to be at a higher level (i.e., more fertilizer, irrigation, herbicides) in order to realize the potential of hybrid seed. In many cases, the less expensive open-pollinated seeds perform better under low and medium input technologies.

The economic success of production depends on the ability to produce and deliver a crop to market on a timely basis. This, in part, depends on getting the crop to its market destination at a time when there is minimal competition from other sources. Poor timing of farm operations and improper site selection in many CBI countries leads to lack of continuity in supply and missed market opportunities. Lack of knowledge of plant habit manipulation (pruning, training practices) is a severe limitation on many CBI tropical fruit growers.

Production constraints are also a common problem for U.S. growers. Land Grant universities in the Southeast allocate millions of dollars and numerous scientist years to carry out research and develop information to be given to local growers on soil modification, irrigation and soil drainage technology, prevention of soil salinity, plant spacing, fertilization, crop rotation sequences to minimize pest buildup and chemical residue carry over, and training/pruning practices to optimize plant form for maximum yield. These applied research programs conducted by

U.S. universities have been an integral part of the U.S. horticultural crop industry success story over the past 100 years.

Fruits and vegetables on hundreds of soil types in the Southeast are grown. Soil type and pH affect yield and crop quality. Most fruit and vegetable crops are more productive on particular types of soil. Root crops are affected by the physical properties of the soil. Carrots grown on heavy clay soils tend to be short and misshapen. In order to obtain maximum yields, CBI and U.S. producers need to be more knowledgeable about how to select crops to match the soil type.

Another common problem is utilization of soils with the incorrect pH. Most horticultural crops require a pH of 6.5 to 6.8. Inadequate application of lime or sulfur to amend the soil pH is a factor limiting yield potential. Growers are not always knowledgeable about the amount and timing of fertilization applications, or about how to counteract deficiencies in various major and minor elements that restrict yield. The interaction of soil fertility problems with deficiencies or excesses in soil moisture result in serious plant stresses which adversely affect yield.

U.S. growers are often faced with frost protection problems, a problem that is also common to Central American growers at higher elevations. Mulches, tents, row covers, and sprinkler irrigation can help warm the soil and air around the plants and protect them from cold temperatures.

SECTION III

RESEARCH AND DEVELOPMENT IN THE CARIBBEAN BASIN REGION

Section II identified the priority common problems that face Caribbean Basin producers of tropical horticultural crops. This section assesses the level of activity of research and development (R&D) on the priority common problems with development including both technology transfer and education.

Based on information available in secondary documents, the site visits to research and education institutions in the Caribbean Basin region, and interviews with key informants, the status of R&D on common problems facing Caribbean Basin horticultural crop producers was assessed (see annex 8). Each common problem was rated in terms of the extent to which the institutions reviewed are responding to each of the common problems identified, with the ratings assigned in terms of three levels of activity (limited, some, and considerable).

For the interested reader, the appendix provides a brief introduction to the institutions reviewed; however, the analysis does not cover the great variety of private sector organizations that carry out technology development and transfer activities for horticultural crops.

Support for research on and development of horticultural crops in the Caribbean Basin region is not new. For example, in the case of melons, much of this research over the years has been carried out by individual entrepreneurs or by organizations, including multinationals (e.g., United Brands), independents (such as Central American Produce Company), and farmer cooperatives (Byrnes, 1989). This technology development and transfer process occurs in a similar manner for other crops such as berries, asparagus, and winter vegetables. Also, a great deal of research is carried out by seed companies and suppliers of other agricultural inputs such as fertilizers and pesticides, including herbicides and insecticides.

While the private sector has been active in developing adaptive research on horticultural crops in the Caribbean Basin region, public sector research and education organizations in the region have focused primarily on traditional food or import substitution crops. Yet, as Table 2 shows, there are many examples of collaborative research on horticultural crops by national or regional organizations, U.S. universities, and others (e.g., the USDA). More recently, research interest in CBI countries has been stimulated by various projects, primarily supported by donors but also by investment initiatives of agricultural entrepreneurs within the region.

Table 2. Examples of past or ongoing research and extension projects on horticultural crops.

* Macadamia--Research started in Costa Rica in 1966 with help from IICA, University of California, University of Hawaii, and others. In 1988, with U.S.A.I.D. support, greater emphasis was placed on the export marketing of macadamia.

* Germplasm--IICA/CATIE have collected germplasm of 400 species. Most of the collection is related to traditional crops, many of which are of significant economic importance.

* Integrated Pest Management (IPM)--In 1984, U.S.A.I.D./ROCAP began an IPM project with CATIE; this activity is now being expanded in the region, including participation by EAP, FHIA, and PROEXAG.

* Caribbean Food Crop Society (CFCS)--This network has existed for 25 years, providing a forum for the exchange of information on research and extension through annual meetings.

* University of Florida (UF)--UF has worked more than 30 years with the Pan American School of Agriculture (EAP), Honduras, in training, faculty exchange, and institutional development.

* The University of the West Indies (UWI)--U.S.A.I.D., in cooperation with the Midwest Universities Consortium for International Activities (MUCIA), collaborated with UWI in strengthening a regional agricultural extension program during a 10-year period.

* CARDI--This organization has received extensive support from U.S.A.I.D. and U.S. universities in research and extension and improved management of the institution.

* Caribbean Basin Advisory Group (CBAG)--This program was authorized in 1966, with the initial funding allocation made in FY 1974. CBAG supports research in tropical and subtropical agriculture by U.S. universities working in collaboration with Caribbean universities.

* IICA and the Caribbean Development Bank (CDB)--In response to the Crop Diversification program of OECS countries, these two organizations conducted a major study on fruit crop development for domestic and export markets.

* FHIA--A.I.D. support to this private agricultural research organization in Honduras is aimed at crop diversification includes a focus on horticultural crops.

Further, the Ministries of Agriculture in several countries have designated certain crops as priorities for export. But in most instances this interest has not progressed to specific research plans or their implementation. This is due to a number of reasons, including underfunded programs, limited training, and emphasis placed on subsistence food crops (e.g., grains), traditional export crops, and import substitution crops. Consequently, very little research has been undertaken on horticultural crops. Accordingly, transfer of technology from public sector research for such crops has been minimal.

Large multinationals and major independent companies are involved in adaptive research as well as technology transfer for horticultural crops; however, the information generated is often proprietary and generally not being tapped by or made readily available to the public except through product sales.

Most of the national research institutions, especially in Central America and the Dominican Republic, have initiated some research related to horticultural crops. FHIA in Honduras, ICTA in Guatemala, and ISA in the Dominican Republic have demonstrated capability, particularly at the production level. However, none of the research institutions has significant levels of research in postharvest handling, transportation, or market penetration.

National universities generally allocate limited resources for research and education on horticultural crops; where research is underway, it generally is being conducted in production areas such as pest management. Postharvest handling technology, transportation, and marketing areas are not adequately covered.

Other institutions in the CBI countries are involved in research or extension work, but were not investigated during this study because of time limitations. A few are doing research and training on horticultural crops. For example, ICAITI has been developing processing and food science technologies. This is a very important area for establishing a competitive edge for CBI countries.

Export development agencies in the region (CAAP, Gremial, FPX, and FUSADES) are relatively new. They were not designed and are not geared to carry out research but, in some cases, have undertaken a small amount of research through contracts, primarily with universities and consultants. Their strength lies in assisting potential growers to link up with buyers and importers in destination markets, to tap into existing technologies in the United States, and to assist in carrying out adaptive trials as part of their export development programs.

The lack of a transfer system for research and extension information within and across countries is one of the most serious problems in the Caribbean Basin region. One key aspect is the validation of technology at the local level. Some technology packages have disrupted traditional farming systems, causing more harm than good. The lack of efficient transfer of information and technologies is a principal factor limiting the production and marketing of horticultural crops.

While IICA has a presence in the Caribbean, Central America, and the United States, it is not involved in hands-on production research, as it works primarily on developing institutional systems for the generation and transfer of technology through research and training. A primary focus of IICA's efforts is agricultural research management and organization. IICA also has a marketing program that focuses on international trade and policy issues as well as the emerging NTAE area.

CATIE is the primary research and graduate training institution in Central America; the University of the West Indies plays this role in the Caribbean. Both institutions have limited involvement in direct extension. CATIE utilizes pilot project areas and education as tools for technology transfer. The EAP (El Zamorano) is dedicated principally to training but also has been developing research and education programs on IPM. It also is in the process of expanding a research program related to postharvest handling and processing.

In the Caribbean, CARDI is primarily responsible for the transfer of technology but has limited emphasis on horticultural crops. CARDI's strategic plan places greater emphasis on horticultural crops, in order to develop technology that will help countries in the region to increase foreign exchange earnings. Under the Agricultural Research and Extension Project (AREP), A.I.D.'s Regional Development Office for the Caribbean (RDO/C) will be providing funds to strengthen CARDI's efforts in research and extension on horticultural crops. This is part of an overall diversification effort in the region. Over the past decade, the University of the West Indies developed a strong extension training and communication support capability under the A.I.D.-funded Caribbean Agricultural Extension Project (CAEP), although this project was aimed primarily at subsistence food crops.

PROEXAG (in Central America) and CATCO (in the Caribbean) are the main regional initiatives focusing on horticultural crops with a market-led approach. Much of their activities are focused on postharvest handling, transportation, and market penetration problems. Contrasted to the aforementioned research and education institutions, these organizations focus on commercial marketing business and export market development.

With respect to U.S. universities, several characteristics are summarized here:

- U.S. universities are strong in all areas of horticultural crops, having carried out considerable research, teaching, and extension on all aspects of fruit and vegetable production, postharvest technology, crop selection, pest management, food processing, and technology transfer. Efforts in these areas have included ongoing projects over the past 100 years in Colleges of Agriculture. There is little duplication of research on horticultural crops, although educational and extension programs are similar among universities.

- With the exception of market analysis and related policy issues, U.S universities are weak in the areas of transportation and market penetration.
- Due to the size of their fruit, vegetable, and ornamentals industries, the University of Florida and the Texas A&M University have the strongest research, education, and extension programs in horticultural crops.
- The University of the Virgin Islands and the University of Puerto Rico at Mayaguez have considerable strength in the area of production problems but limited expertise in the postharvest handling, transportation, and marketing fields. Both universities, as well as the University of Florida, have been involved in research in the Caribbean Basin region through the CBAG program since 1974, although very limited joint research has been focused on the marketing of horticultural crops.
- The USDA facilities in South Miami (Homestead) and Mayaguez have extensive research capabilities in production and plant protection with little or no capabilities in postharvest problems.

Another important area reviewed concerned the links between national research institutions within and between countries and the relationships between universities throughout the Caribbean Basin region. The University of Florida has by far the strongest link with Central American and Caribbean research and education institutions, addressing the multiple common problems of horticultural crops. However, all states abutting the Gulf of Mexico have some cooperative research, education, and training programs with institutions in the CBI countries.

Overall, there are many research, extension, and educational institutions in the CBI countries and the U.S. states abutting the Gulf of Mexico. However, with respect to successful development of horticultural crop industries, the study found that:

- The three priority common problems--production constraints, plant protection, and harvesting/postharvest technology and management--are not being addressed adequately by public research and education institutions in the CBI countries.

- The limited research and education on horticultural crops underway in the CBI countries primarily is carried out by the private sector; however, much of the technology deriving from this research is proprietary and not widely disseminated.

- The public sector research/education institutions that are becoming involved in research on horticultural crops often are not effectively linked with existing private sector agricultural research on horticultural crops.

- Overall, across the three Basin sub-regions, there is very little coordination of research and education on horticultural crops.

- Generally, CBI and U.S. horticultural crop producers do not have an effective forum for discussing and setting research priorities or for disseminating the results of research to horticultural producers.

In view of the growing markets for horticultural crops, these three common problems should receive greater attention in terms of joint research and education. However, over the long run, establishment of research priorities needs to be a dynamic, interactive process between technology users and technology suppliers.

In short, there is a need for improved links and communication between technology suppliers and users in a way that facilitates research on problems of common concern. This can be stimulated by a mechanism that (1) ensures systematic dialogue between public and private research and educational institutions; (2) strengthens the role of the private sector in establishing research priorities and in providing research funding support; and (3) facilitates technology transfer to horticultural producers through education, extension, and other means as appropriate.

Given the differences in the scale of operation between CBI and U.S. producers of tropical and sub-tropical horticultural crops, care needs to be taken that any mechanism to facilitate joint research and education on common problems leads to shared benefits.

SECTION IV

POTENTIAL BENEFITS OF JOINT RESEARCH AND EDUCATION

A. Need for Joint Research

Most Caribbean and Central American nations are small and find it difficult to support comprehensive programs in agricultural research and education. This situation is even more marked in the islands of the Caribbean, where even fewer nations than in Central America are sufficiently large to support more than minimal agricultural research and education programs. In both Central America and the Caribbean, regional institutions such as CATIE and CARDI, respectively, have evolved to assist the nations within each of these two regions in developing agricultural research and education programs. Despite the presence of such regional institutions, many gaps still exist in the capacities of CBI countries to do the research and education essential for supporting development of horticultural crop industries.

Generally, joint research allows for specialization, thereby reducing duplication as well as research costs, a factor that is a concern to U.S. as well as CBI producers. Specifically, for U.S. producers, implementing agricultural research on a joint basis makes it possible to conduct research year round, thereby reducing the amount of time needed to generate results.

A report on "Agricultural Research in the Caribbean" (Trigo, 1988), published by IICA's Technology Generation and Transfer Program, points to the benefits of a cooperative coordinating mechanism for strengthening agricultural research and education programs of a group of countries. Some coordination systems (networks) have been created through donor support in concert with countries in a region, although these networks are aimed primarily at supporting/developing research on traditional food crops.

The implication for strengthening research and education on problems of common concern to Caribbean Basin producers is that strong consideration needs to be given to facilitating the coordination of collaborative or joint research and education on horticultural crops. There is reason to believe that much progress has already been made in this sphere for traditional food crops, but comparable initiatives for horticultural crops are lacking.

B. Potential Benefits of Joint Research

While quantitative data on the exact magnitude of economic benefits of joint research and education could not be developed within the time frame provided for this study, past research on returns to investment in agricultural research suggests that the potential economic benefits to CBI and U.S. horticultural producers of joint research and education on problems could be very large. Supporting data are provided in annex 10. The limited data available from various economic analyses indicate that further research and education on horticultural crops are desirable and that the payoff to such investment in research and education would be high, with a higher return than development efforts in many other sectors.

As an example, a recent study (Ansoanuur, 1988) on returns to postharvest research and development in the winter tomato industry found that postharvest expenditures have a very high rate of return, with growers and distributors receiving 33 percent of the returns and consumers 67 percent. For every additional dollar of pre-harvest research investments, the societal surplus increased by $10.85. For postharvest research investments, the societal return was $12.70 for each additional dollar of investment. The net average rates of return showed a similar pattern of distribution. On average, society received $348 for research investments made prior to harvest; postharvest research returns were greater.

As the United States faces the future, Secretary of Agriculture Yeutter is emphasizing competitiveness as the strength of U.S. agriculture. In testimony before Congress on the 1990 farm bill, he noted that research, education, and technology are the means to maintain competitiveness. Frank Press, as president of the National Academy of Sciences, stated that scientific exploration has intrinsic cultural and intellectual values of the deepest kind and that it deserves support on these grounds. "However," he said, "the large resources allocated by governments and industries to scientific research find their justification on the more pragmatic grounds of national economic and political security."

Support for additional agricultural research on horticultural crops will, on the basis of the available evidence, contribute to the expanded agricultural development and welfare of all three sub-regions of the Caribbean Basin. With this in mind, the following section highlights examples of potential economic benefits that CBI and U.S. horticultural industries could receive from a joint program of research and education on the problems identified as common to Caribbean Basin and U.S. producers of horticultural crops.

1. Plant Protection

Basic knowledge developed on identification, characterization, epidemiology, and control of pests and diseases (particularly viruses) would be beneficial to the CBI countries and the U.S. Southeast. Improved knowledge of the distribution of specific pests and diseases in Central America and the

Caribbean would assist efforts to exclude them from the United States, thereby protecting existing agricultural industries.

Eradication of fruit flies from a given country would have the benefit of eliminating crop losses and would result in the relaxation of export constraints on countries that restrict products from fruit fly areas. Economic losses to Guatemalan growers of mango, orange, pear, and peach due to fruit flies were estimated at $7.5 million in 1987.

There is a dearth of research on accurate estimates of crop loss data. Joint research on possible non-chemical control methods has universal applicability. Parasitic or predatory organisms native to one region may be found and used in biological control programs for other regions. Agriculture in the U.S. Southeast could benefit greatly from research on biological control in the CBI countries. Many of the important horticultural pests have been introduced or are annual immigrants from the tropics. Further introductions are also a constant threat. It is a well-established principle that such pests are subject to a wider range of biotic control agents in their geographic areas of origin than in areas where they are introduced.

Further research is needed to determine the pathways and the biology of the migration of pest species. Such research, which will provide the knowledge needed to understand how pest population dynamics in the tropics affect the U.S. pest problem, is essential before complete management systems can be developed. Joint research of scientists in CBI countries and the U.S. Southeast would expedite solving many pressing entomological and pathological problems.

2. Harvesting/Postharvest Technology and Management

Joint benefits of research and education in determining optimal harvest maturity stages would provide for stronger year-round markets. Superior product taste and quality can be achieved only by harvesting at the ideal development stage. Maturity indices need to be defined (i.e., soluble solids, starch content, acidity, color) for optimal harvest stage of many crops. Educational efforts are needed to avoid physical injuries from improper picking, handling, and packing procedures.

Postharvest technology is a very problematic area for all horticultural businesses in the Caribbean Basin region, and it is also a major common problem for U.S. growers. In some cases, the optimum storage temperature and humidity conditions have not been clearly established for exotic tropical horticultural products. Joint research between U.S. and Caribbean institutions would benefit industries in both areas. Lack of rapid removal of product field heat results in rapid ripening and deterioration. Thus, product quality and nutritional value are negatively affected. The optimal method of pre-cooling, whether by forced air, hydrocooling, slush-icing, or vacuum cooling, has not been identified for many of the tropicals. Joint research on mechanical electronic grading systems to maintain uniform product quantity as well as on containers and packaging materials to minimize product bruising would benefit all growers.

Maintaining product quality control is often lacking in packinghouses because personnel are not trained. In many CBI countries, quality considerations are of little importance in domestic food marketing systems. This not due to the lack of appreciation of good quality produce; rather the economic benefits for applying high grades and standards are not evident. Changing the inadequate grading practices of indigenous laborers hired to work in export packing sheds is a difficult managerial challenge. Compliance with improved standards of quality and more rigorous grading procedures requires continuous education and supervision of the labor force.

Certain tropical commodities should not be stored below 12 to 15°C, in order to prevent physiological damage due to chilling injury. Joint research on the postharvest physiology and biochemistry of tropical commodities will provide an understanding of the exact storage requirements for each crop and the consequences in loss of quality and marketability suffered if growers do not adhere to optimum postharvest conditions. Certain commodities are very sensitive and adversely affected by ethylene gas, a natural ripening hormone. Joint research on individual commodity sensitivities would benefit mixed load shipments from both the United States and the Caribbean Basin countries.

Many subtropical and tropical horticultural products cannot be exported because of fruit fly quarantine restrictions. Joint research on identification of the optimal plant quarantine treatment methods to satisfy the phytosanitary requirements of importing countries would benefit Caribbean Basin growers who export to the United States during the domestic off-season and U.S. growers exporting to Pacific Basin countries.

Strategies for postharvest pest and disease control should employ an integrated preventive approach, including sanitation, postharvest chemical treatments, modified atmosphere packaging, and management of such improvements in commodity system.

3. Production Constraints

Many growers need assistance with land use, terracing, soil conservation, fertilization requirements, mulching, and planting of cover crops. Joint research in these areas would be beneficial to all producers. Prevention of soil erosion preserves the global ecosystem. Improved technology from joint research on the fate of nitrogen fertilizers in different soil types would allow for better fertilizer management and protection of ground water from nitrate contamination, a serious hazard to human health.

Two of the most limiting factors on crop production for U.S. growers are inadequate fertility practices and improper irrigation practices. Research on identification of proper fertilizer placement, rate, and timing for each individual crop and/or variety would benefit growers throughout the Caribbean Basin region. Many growers currently use too little or too much fertilizer and suffer yield losses. Salt burn is a common problem resulting from fertilizer misapplication; and buildup of soil salinity is becoming more serious as growers in the United States have restrictive water utilization rights.

Research is needed on water use rates of horticultural crops under different environmental conditions. Establishing the threshold moisture levels at which yield or quality reductions occur in each crop could help all growers decide if the expense of irrigation justifies the benefit. Research also is needed on the optimal and most economical irrigation methods for specialty crops produced both in the United States and in CBI countries.

Public consciousness of chemical use by the farming community has been elevated in recent years. Production without chemicals is difficult, but not necessarily impossible. Research to establish the proper crop rotation sequence or intercropping systems to minimize weed and pest pressure would benefit all horticultural growers; little research has been done on this.

Utilization of different mulches (organic, plastic, paper) may result in higher fruit and vegetable crop yields due to more uniform soil moisture retention, weed control, and sanitation against soil-borne disease. Further research and development of this technology may result in preservation of soil structure, minimal soil erosion, and better crop yield and quality. Photodegradable mulches offer a potential solution to environmental waste and need to be researched under many different microenvironments to establish the optimal type to use in each region. Use of mulches for fruit and vegetable growing is beneficial to yield and quality. Research in this area would be beneficial to growers in both the CBI countries and the United States.

Manipulation of the production cycle of a plant will allow products to be available during the market windows. Research on plant growth regulators and their effect on the flowering/fruiting processes would provide for more year-round product availability. Frost protection research is needed to extend marketing periods. Utilization of plastics for this purpose offers great potential, but research in this area is in its infancy.

With the ever-changing availability of agricultural chemicals, research on identifying the optimal plant spacing, population density, and plant growth habit would benefit both CBI and U.S. growers. Research on production practices for producing optimal economic yields also would be beneficial.

SECTION V

IMPLEMENTING JOINT RESEARCH AND EDUCATION

A. Five Options Considered

There is a need for improved coordination of research and education on horticultural crops in the Caribbean Basin region. Improved coordination can be achieved by establishing a collaborative network that would provide opportunity for involvement of public as well as private actors in research and education on horticultural crops. What mechanism could provide an effective means to support joint research and education on the common problems identified? Table 3 identifies five options.

Table 3. Five Options Concerning Support for Joint Research and Education on Identified Priority Common Problems.

No Intervention Option--Agricultural research and education in the Caribbean Basin continue to function as is without any intervention.

Option A--Establishment of a collaborative research and education center as a new organization.

Option B--Establishment of a collaborative research and education center as a new organizational unit in an existing institution.

Option C--Strengthening research and education programs of and networking among existing, largely public, institutions, with funding provided directly to the institutions and the private sector playing an advisory role in how these funds are allocated.

Option D--Implementing a private joint research and education program coordinated by an international horticultural industry group, with funding provided directly to this group which, in turn, would allocate funding to the institutions.

Each option was evaluated in terms of staffing pattern, coordination, likely impact, and cost, although information availability and time restrictions precluded analysis of the specific cost of each option. Given the identified need for joint research and education, the first option, little or no intervention was ruled out. Options A and B provide for the creation of a new organization or a new unit within an existing organization, respectively, while Option C focuses on strengthening research and education programs of existing organizations, the majority of which at both the national and regional levels are public institutions. Some of the relevant points regarding these options are now considered.

Significant cost limitations are associated with establishing a new research and education center (option A). Indeed, horticultural producers throughout the Caribbean Basin region were fully in agreement that no new agricultural research or education centers should be established. They feel that existing research and education institutions should become more responsive to the problems horticultural producers are facing.

While establishing a new organizational unit in an existing research and education center (option B) would be less costly than establishing a research and education center as a new organization, the apparent need is for getting existing research and educational organizations to collaborate more effectively; there was no apparent reason to believe that establishment of a new research and education center within an existing organization would be the most effective means of responding to this need.

Option C focuses directly on the question of improving the coordination of research and education among existing, largely public, institutions, proposing sub-regional coordinating roles for a designated institution within each sub-region (e.g., CATIE in Central America) and an overall or regional coordinating role for IICA. However, the private sector's role in this option is largely advisory, with little if any direct control over setting research priorities, allocating research funds, or disseminating research results. Further, implementation of this option could be impeded by inertia, all of these research, education, and technical assistance institutions basically being public sector organizations that simply cannot respond as quickly or as flexibly as the private sector.

A further consideration is that horticultural producers in the Caribbean Basin region, but particularly in the U.S. Southeast (e.g., Florida), have expressed a desire to form a private non-profit association that would facilitate the producers in:

- Establishing an agenda for research and education on the common problems faced by horticultural producers in the Caribbean Basin region;
- Communicating this agenda to agricultural research and education institutions in the region; and
- Translating research findings into practice through improved dissemination of findings and technologies developed through research.

In light of these considerations, option D provides for the research funding to be channelled through a research and education program coordinated by a private international horticultural industry group, thereby linking technology users in the private sector and researchers in the public and private sector, with the private sector having direct control over the setting of research priorities, allocation of research funds, and dissemination of research results. At the same time, by providing support for agricultural research, this option serves to strengthen and to improve coordination of public sector research and education on horticultural crops. To the extent that it would be desirable, this option also could provide a means for the private sector to play a greater role in funding research on horticultural crops.

B. Conclusion

While the scope of work for this study did not provide for a systematic review of horticultural crop research underway in the private sector in the Caribbean Basin region, the report provides sufficient information to conclude that option D, that of establishing a private coordinating body, comprising Caribbean Basin horticultural producers and mandated to fund and coordinate joint research and education among existing Caribbean Basin research and education institutions, would provide an effective means for implementing joint research and education on common problems facing horticultural producers in the Caribbean Basin region.

Further, the report recognizes that a systematic review and analysis of private sector horticultural research could provide an important input to making a final decision about the most appropriate approach for investment aimed at facilitating joint research on the common problems facing CBI and U.S. horticultural producers. However, the reader should bear in mind that data on private investment in agricultural research are very difficult to obtain even in the United States.

The following section considers the functions, sustainability, and expected impact of option D.

1. Functions

This option would establish a private, non-profit horticultural industry group (or association) composed of the growers, packers, processors, shippers, transporters, and importers in the international horticultural market, including the growers and exporters of horticultural crops in the Caribbean Basin region. The association's work would be assisted by a Research and Education Advisory Council (REAC) composed of representatives of Caribbean Basin agricultural research and education institutions.

As conceived by the producers, the association's mandate would be to assist horticultural producers in the Caribbean Basin region in developing domestic and export markets for horticultural crops, including fruits, vegetables, and ornamentals. This mandate would include setting priorities for the funding, coordination, and dissemination of the results of joint research on common problems facing the horticultural industry in the Caribbean Basin region. This program would be implemented through a series of competitively-let research contracts.

The association would have as its prime objectives, (1) evaluation of common problems facing horticultural industries in the Caribbean Basin region; and (2) support of research, technology transfer, and other activities designed to solve priority problems and disseminate research results (e.g., technology) to industry participants, including growers, packers, processors, shippers, transporters, and importers. The association, supported by member participation and assisted by the Research and Education Advisory Council (REAC), would:

- Identify and prioritize common problems that need to be addressed through joint research and education;
- Circulate a research needs agenda soliciting proposals from public and private research organizations to carry out research on the agenda's priority common problems;
- Review the research proposals submitted and fund the proposals selected;
- Monitor research implementation and review the reports submitted by the contracted researchers; and
- Disseminate research findings, conclusions, and recommendations among association members throughout the Caribbean Basin region.

The association would work with a range of participants in tropical fruit, vegetable, and ornamental industries to support development of tropical horticultural markets through:

- Industry representation, promotion, and market development;
- Industry negotiation with the Environmental Protection Agency (EPA), USDA (APHIS), U.S. customs, and other governmental regulatory organizations;
- Business development (fostering joint ventures);
- Identification of priority common problems for research and development; and management of funding for industry-wide research;
- Collection and dissemination of production and marketing statistics on the horticultural industry; and

- Publication of a newsletter reporting industry news, statistics, and association-sponsored research.

2. Sustainability

Funding support could come from a mix of sources, including member associations and commercial firms in the private sector (multinationals, ocean freight companies). Initially, start-up funding for a pilot program (e.g., five years) would need to be provided by interested donors. Based on favorable evaluation of the program, additional funding could be provided on a matching grant basis during the program's next five years (years 6-10). During the program's sixth year, donor funding could match 80 percent of the research funds privately raised by the association, with matching grants during years 7 to 10 declining as follows:

Year	Percentage Matched
7th	60
8th	45
9th	30
10th	15

Donor funding during program years 6 to 10 could be made contingent on the association having put into place a mechanism for developing the organization's self-sufficiency. In other words, by a designated target date (e.g., program year 3), the association would implement a program (a check-off system) whereby growers would be assessed a determined per-box amount (e.g., US$.01) on each box of produce sold in the marketplace. The monies generated would be used to create a fund to support the association's research program. Thus, disbursement of matching grant funds would facilitate development of a self-sustaining mechanism to finance ongoing research and education on the common problems most affecting horticultural crops in the region.

If this mechanism proved, during its start-up period, to be beneficial to the development of the tropical fruit, vegetable, and ornamental industries in the Caribbean Basin region, as evaluated by these industries and donors, then additional funding for support of the program would be expected from the private sector. The level and eventual termination date of donor funding would be phased according to a predetermined time schedule. Evaluations of the program would be done every two years, with required adjustments made on the basis of the experience gained.

3. Expected Impact

The proposed mechanism would not only have a strong impact on the nations within the Caribbean Basin region, including U.S. growers and market participants. Implementation of option D also should result in highly improved research and education competence within the research institutions that participate in the development of research and education programs supported by the association. Researchers in CBI countries would be afforded the opportunity to cooperate with U.S. researchers in developing solutions to problems and to interact and exchange information with U.S. research and education specialists participating in the program.

Of course, U.S. researchers would benefit from collaborating with specialists throughout the Caribbean Basin region. Overall, this mechanism should greatly facilitate exchange of market-relevant technology and information in the region. Thus, links between CBI and U.S. technology development and transfer institutions could be improved without creating another new research center or institute.

The requirement in option D that research proposals provide for joint collaboration of research and education institutions in CBI countries and the U.S. Southeast would facilitate exchange of technological information throughout the region. While extension services in the United States are generally effective in disseminating the results of research, public extension services in Central America and the Caribbean have yet to reach peak effectiveness. Option D would strengthen the ability of the private sector throughout the Caribbean Basin region to disseminate research findings to market participants, including growers, thereby complementing technology transfer by public extension services.

C. Some Additional Considerations

In the long run, linking option D with a donor-funded network of public research, education, and technical assistance organizations would provide an additional impetus to technology generation and transfer across the Caribbean Basin's three sub-regions. However, this would require ongoing reorientation of the research priorities and approaches of public sector organizations toward an increased emphasis on research geared to the production constraints on and market opportunities for horticultural crops. In the short run, the implementation of option C would serve to begin this reorientation process within the public sector.

Given current difficulties in sustaining funding for public sector research and education institutions in the Caribbean Basin region, option D would enable the private sector in the region to quickly mount a systematic and coordinated research and education program on common problems facing horticultural growers in the region. With this mechanism in place, donor agencies (WB, IADB, CDB, A.I.D., etc.) could effectively target funding support for developing tropical horticultural crops throughout the region. Improved research and education on common problems constraining market development of these crops would increase the range of production and marketing options for all agricultural producers, including those who are primarily or solely subsistence farmers. Indeed, the potential positive impact that developing horticultural crop markets could have on the income-earning potential of subsistence farmers points to the need for donors to allocate more resources to the cultivation of this opportunity.1/

In the final analysis, the private sector plays and should continue to play a lead role in developing horticultural crop industries, especially in the case of horticultural crops in the CBI countries. Virtually all the plant protection, postharvest handling, and production technology for horticultural crops such as melons, berries, winter vegetables, and asparagus has been adapted by the private sector through on-farm research. These are the same major problems identified in this study as the priority common problems facing Caribbean Basin producers. While some research can be done by the private sector, especially where a profit can be made, there is a need for additional research on horticultural crops that can be achieved only by greater involvement of and participation by the public sector, especially in basic or applied research and the collection of generic data.

1/von Braun, Hotchiss, and Immink, Nontraditional Export Crops in Guatemala: Effects on Production, Income, and Nutrition, Research Report 73, IFPRI, Washington, D.C.

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APPENDIX

OVERVIEW OF RESEARCH AND EDUCATION INSTITUTIONS IN THE CARIBBEAN BASIN REGION

Annex 7 of the JAREF Study Technical Report provides the research mandate and detailed information on Caribbean Basin research and educational institutions involved in research and/or education on non-traditional agricultural export (NTAE) crops. This appendix briefly familiarizes the reader with the names and acronyms of these institutions. Also provided are acronyms of major A.I.D.-assisted projects and institutions working on NTAE crop development in the region. Other organizations working at the national level in the region not reviewed here include FAO, bilateral technical assistance projects of other governments, and various non-government organizations (NGOs).

A. The Caribbean

The principal sub-regional agricultural research institution in the English-speaking Caribbean is the Caribbean Agricultural Research and Development Institute (CARDI), with headquarters at University Campus, St. Augustine, Trinidad, and research staff and facilities on each of the Caribbean islands. CARDI primarily has focused on basic food crops but in recent years has begun to place increased emphasis on research on NTAE crops. The Faculty of Agriculture of The University of West Indies (UWI), also in St. Augustine, Trinidad, is the main degree-granting educational institution in the English-speaking Caribbean.

The Caribbean Agricultural Trading Company (CATCO), based in Barbados, seeks to increase food commodity trade among CARICOM member states and in extra-regional markets. CATCO is a mixed public/private stock corporation, with 51 percent of its stock held by the Caribbean Food Corporation--a regional organization owned by the 12 CARICOM governments. The Caribbean Industrial Research Institute (CARIRI), in Trinidad, conducts research and development on food technology (e.g., food processing). WINBAN, an umbrella organization for Windward Islands banana producers associations, has developed into a model research and extension organization in the Caribbean.

U.S.A.I.D.'s Eastern Caribbean Mission (RDO/C) is implementing the West Indies Tropical Produce Support (TROPRO) project to provide market information, production, and postharvest handling support for NTAE crop development in OECS countries. Under TROPRO, CARDI will have primary responsibility for research, CATCO for extension. The Inter-American Institute for Cooperation on Agriculture (IICA) (see section III.A.1) has a project, "Strengthening Farmer Organizations in the Windward Islands and Antigua and Barbuda," that seeks to improve the quality of production and marketing services reaching the members of farmer organizations.

Other organizations involved in research and education on NTAE crops in this sub-region include the Agricultural Development Foundation (ADF) and the Superior Institute of Agriculture (ISA) in the Dominican Republic and the Jamaica Agricultural Development Foundation (JADF) in Jamaica.

B. Central America

The Tropical Agricultural Research and Training Center (CATIE), Turrialba, Costa Rica, is an autonomous regional institution devoted to research and education for agricultural development and integrated management of natural resources in CATIE's seven member countries--the Dominican Republic and six Central American countries (Costa Rica, El Salvador, Guatemala, Honduras, Nicaragua, and Panama). CATIE, like CARDI in the Caribbean, has focused primarily on basic food crops but in recent years has begun to place increased emphasis on research on NTAE crops. While CATIE's research mandate is limited to the organization's member countries, CATIE has a Latin American mandate in education (M.S. and continuing education levels).

The Fundación Hondureña de Investigación Agrícola (Honduran Agricultural Research Foundation) (FHIA), in La Lima, Honduras, is a private nonprofit research organization that was created to foster expansion and improvement of technology generation and transfer to meet production needs and export opportunities of Honduran farmers. The Escuela Agrícola Panamericana (Pan American Agricultural School) (EAP), El Zamorano, Honduras, is a private, nonprofit, degree-granting agricultural college.

The Escuela de Agricultura de la Region Tropical Húmeda (Agricultural School for the Humid Tropics) (EARTH), located in Costa Rica, is a four-year agricultural university that will focus primarily on agricultural education for the humid tropics. The school opened for its first class of students in March 1990.

The Federación de Asociaciones de Productores y Exportadores Agropecuarios y Agroindustriales de Honduras (now FPX, formerly FEPROEXAAH), San Pedro Sula, Honduras, is a private agricultural export development organization that provides growers/exporters of tropical fruits, vegetables, and ornamentals with assistance in identifying export projects, developing financial packages for financing, and assisting exporters in postharvest handling, transportation, and export marketing.

The Consejo Agropecuario Agroindustrial Privado (CAAP), San Jose, Costa Rica, is a private organization that seeks to develop a sustainable horticultural crop export industry and to improve product quality to exportable standards. CAAP assists NTAE crop growers in production, pest management, postharvest handling, and marketing. CAAP provides funds to the University of Costa Rica (UCR) for production and processing research on NTAE crops.

The U.S.A.I.D./ROCAP Non-Traditional Agricultural Export Support Project (PROEXAG), in Guatemala City, Guatemala, is working to create and/or strengthen private sector capabilities through the provision of "hands-on" training and technical skills related to production technologies and market intelligence for NTAE crops. PROEXAG assists export federations in four Central American coun-tries (CAAP in Costa Rica, FUSADES in El Salvador, Gremial in Guatemala, and FPX in Honduras) in strengthening their capacity to export non-traditional crops. Assistance is provided in all aspects of production, pest management, postharvest handling, transportation, and market penetration.

The Inter-American Institute for Cooperation on Agriculture (IICA), in San José, Costa Rica, is an international organization for technical cooperation and strengthening of institutions in its 31 member states, including the United States and countries of Latin America and the Caribbean. IICA has five programs, including technology generation and transfer and marketing, the latter including an NTAE component.

C. U.S. States Abutting the Gulf of Mexico

The Caribbean Basin Advisory Group (CBAG) was funded by Congress in 1974 for research on tropical and subtropical agriculture by the University of Florida (UF), the University of Puerto Rico (UPR) at Mayaguez, and the University of the Virgin Islands (UVI). Administered by the USDA, CBAG focuses on two objectives: (1) obtaining readily useful information that will improve production and marketing of agricultural commodities produced in the Caribbean and broaden their research base; and (2) providing information to the United States on critical agricultural problems unique to the semi-tropical area of the U.S. Southeast.

CBAG offers graduate student and post-doctoral level training of Caribbean Basin students at UF, UPR, and UVI. Cooperation on research projects also is given by the USDA subtropical and tropical research stations in Homestead, Florida and Mayaguez, Puerto Rico. The following crops have been identified for high priority research: aroids (root crops such as taro), papaya, and tropical vegetables (sweet potato, potato, tomato). Research emphases include regional testing of tropical fruit cultivars, yams, peppers, and sweet potatoes; pest management; water management; soil and crop management technology; postharvest technology for the tropics; plant stress; insect migration patterns; food processing; and technology transfer improvement.

In 1989, the total budget allocated to research was $1.56 million, with about 55 percent of the grants allocated to the University of Florida, 30 percent to the University of Puerto Rico, and 15 percent to the University of the Virgin Islands. The average grant size was $37,000 for 41 funded projects.

The Animal and Plant Health Inspection Service (APHIS) of USDA is supporting pest surveys throughout the Caribbean to monitor population levels of insects potentially damaging to the commercial U.S. industry. By cooperating with foreign governments, APHIS strengthens plant protection and quarantine activities for pests of concern to the United States. APHIS has cooperated with IICA and the USDA in surveying Grenada and St. Vincent, declaring these islands free of fruit flies, and allowing fruit to enter the United States from these markets without quarantine restrictions.

The USDA Horticultural Research Laboratory, in Orlando, Florida, conducts research on bacterial, fungal, nematode, and virus diseases of citrus and sub-tropical fruits. Areas of research include development of rapid, practical, and economical methods of pathogen identification, disease characterization, biological control of diseases, and characterization of host-parasite interactions and epidemiology. Postharvest research includes developing technologies for increasing shelf life and maintaining quality and condition by environmental manipulation and improved handling methods; and assisting in development of effective, non-toxic quarantine treatments for commodities in the domestic and export markets.

The Tropical Agriculture Research Station (TARS), Mayaguez, Puerto Rico, is part of the South Atlantic Region, Agricultural Research Service, USDA. TARS conducts tropical agricultural research for the benefit of the United States, Puerto Rico, and other countries of the Caribbean Basin by introducing, evaluating, selecting, multiplying, preserving, and distributing germplasm; developing systems to increase food production for local use and export; and developing systems for long-term use, conservation, and management of tropical plants and soils.

The University of Puerto Rico (UPR), Mayaguez, Puerto Rico, is a U.S. Land Grant university. The College of Agriculture conducts extensive research on tropical fruit and vegetable crops within Puerto Rico's various departments. The university also has six Agricultural Experiment Stations located in distinct regions of the island. This provides coverage of various soils and climatic zones representative of the Caribbean. Basic laboratory research is supplemented by applied field production research. The UPR offers undergraduate, graduate, and short-term training in all aspects of NTAE crop production, storage, food technology, and marketing. The campus is physically adjacent to the USDA's TARS, where a number of cooperative research projects are conducted. UPR has excellent cooperative ties with the University of Florida and the University of the Virgin Islands.

The University of the Virgin Islands (UVI), St. Croix, Virgin UPR is a member of CBAG. Islands, is a publicly-supported Land Grant university that offers programs of instruction, research, and public service on NTAE crops. A baccalaureate program is offered in agriculture, with courses in farm management, tropical agriculture, and food preservation. UVI is a member of CBAG.

The Institute of Food and Agricultural Sciences (IFAS) of The University of Florida (UF), Gainesville, Florida, conducts research, teaching, and dissemination of science-based information through the extension service. IFAS research supports Florida's $US 40-billion food, agricultural, and natural resources industries; prepares students for careers in those industries; and delivers technology to consumers on a wide variety of topics.

The Center for Tropical Agriculture (CTA) is a component of IFAS. CTA supports academic departments and faculty in developing tropically oriented courses and degree programs; coordinates interdisciplinary research projects; and plans and arranges administrative, academic, and technical support for domestic and international activities related to tropical agriculture. The Center offers special training programs in agriculture at the UF campus and at Agricultural Research and Education Centers located throughout Florida. The Center is also involved in research in collaboration with Caribbean research and education institutions such as the Pan American School of Agriculture (EAP) in Honduras.

IFAS also operates the Tropical Research and Education Center (TREC) at Homestead, Florida. This unit has 17 faculty positions in entomology, plant pathology, genetics, tissue culture, and fruit and vegetable horticulture. Most of TREC's research is commodity-oriented, including but not limited to winter vegetables (tomato, bean, potato, squash, etc.), boniato, yucca, melanga, calabaza, tropical fruits (lime, avocado, mango, annona, carambola, papaya), and sugar cane.

For at least 20 years, scientists at TREC have cooperated with scientists in the Caribbean including personnel at CARDI, CATIE, IICA, and EAP. Cooperative studies with scientists in the Dominican Republic, Puerto Rico, and the French Islands are in progress. For several years TREC scientists have been recipients of grants addressing Caribbean research problems under the CBAG program of Special Grants administered by USDA/CSRS.

The Food and Resource Economics Department (FRED), a part of IFAS, is developing the International Agricultural Trade and Policy Center (IATPC), which is aimed at expanding Florida's comparative advantage in tropical and subtropical agriculture on a resource-sustaining basis. Specific attention will be directed to improving the U.S. agricultural trade position generally and to Florida's competitive position in domestic and foreign markets for agricultural products and services.

FRED has been involved, under a USDA/CBAG grant (1987-90) in a study called "Intra-Caribbean and U.S. Agricultural Trade:

Implications for Development." During 1988-89, the department carried out a study on the Latin American/Caribbean Debt Crisis Effects on Aggregate Trade Flows and Florida Agriculture. As a follow-up to these studies, the department is projecting funding under CBAG for studies on the Caribbean Basin Debt Crisis, Agricultural Trade, and Agricultural Diversification; and Economic Feasibility of Producing Specialty Crops in the Caribbean Basin.

The Louisiana State University (LSU), Baton Rouge, Louisiana, is a Land Grant university. LSU's College of Agriculture conducts research on NTAE crops in the areas of breeding, plant protection, crop production, postharvest technology, processing technology, and marketing. LSU engages in cooperative research with the USDA, FHIA (in Honduras), and the UPR (in Puerto Rico), primarily in the areas of pest management and germplasm development for vegetable crops. LSU has strong links to Jamaica in developing a new agricultural university. LSU offers undergraduate and graduate degrees in all aspects of fruit and vegetable crops, including plant breeding, crop production, pest management, food processing, and marketing. LSU is recognized as a leading pest management research center.

The Texas A&M University (TAMU), College Station, Texas, offers undergraduate and graduate training in many aspects of horticultural crops (breeding, crop production, pest management, marketing, and food technology). Research is conducted on crop improvement, plant protection, food processing, and marketing. Cooperative research programs exist between TAMU faculty and the private sector within Texas and Mexico. TAMU has cooperative projects with FHIA on melon virus control research and with USDA-TARS, Mayaguez, Puerto Rico, on starchy root crop genetics.

TUESDAY, MARCH 27, 1990.

HELPING CHILDREN AND REFUGEES

PUBLIC WITNESSES

KUL C. GAUTUM, DIRECTOR OF PLANNING, UNICEF
LAWRENCE E. BRUCE, PRESIDENT, U.S. COMMITTEE FOR UNICEF
PHYLLIS DOBYNS,, SENIOR VICE PRESIDENT, SAVE THE CHILDREN
NEIL BOOTHBY, FORMER DIRECTOR, SAVE THE CHILDREN
REV. THOMAS HARVEY, EXECUTIVE DIRECTOR, CATHOLIC CHARITIES
ROGER P. WINTER, DIRECTOR, U.S. COMMITTEE ON REFUGEES

CHAIRMAN'S OPENING STATEMENT

Mr. McHUGH. Gentlemen, I think we will get started. Thank you very much for being with us this morning.

Let me first apologize on behalf of our chairman, Mr. Obey, who unfortunately has a bad case of laryngitis and was up half the night. So I will be sitting in. It is a privilege for me to do so, and I know Mr. Obey is very sorry that he cannot be with us this morning. He has prepared an opening statement which I would like to read on his behalf, and then we will recognize each of our witnesses for their statements and go to questions.

This morning the committee will embark on a new hearing aimed at examining the issues and funding associated with our two most vulnerable recipients of U.S. foreign aid, children and refugees. This year the committee is going for quality rather than quantity in hearings, and we have selected the issue of children and refugees as one that deserves emphasis and highlighting. This is because both of these groups are in a sense at the mercy of programs and assistance that must take place before they are able to help themselves.

More than 50 percent of the population of most countries that are receiving U.S. foreign assistance are children. The worldwide refugee population is now estimated to be 14 million, of which 60 percent are children.

Although progress was made in the 1970's and '80's in helping children, UNICEF in its annual report estimates that more than 100 million children will die from illness and malnutrition in the 1990's if current trends are not changed. Children are being caught up in events that they have no control over. Debt payments and military spending are estimated to absorb half of the third world countries' annual expenditures. There is little, if anything, left over to help children and adults survive.

Military conflicts in Mozambique, Sudan, and other countries leave children homeless and at risk. Our own programs in the United States are now caught up in varying policy directions, structural adjustment, economic reform, cash payments, sectoral spending, economic jump starts, and so on. These programs may be necessary to help countries be stable enough to help their people, but they alone only lull us into false security that something is happening to help children and others not in the mainstream of economic reform.

Health, education, and international programs such as UNICEF should be promoted along with economic programs, not sacrificed for economic programs.

Let us look at where the Administration puts its money this year. Overall, there is a program increase of about $800 million over last year. Military spending increases by $345 million and the economic support fund by $250 million. At the same time, development programs are experiencing a slight decrease.

Funding for refugees between the regular account and the emergency fund is up a net of $40 million, but in the context of the $70 million pending supplemental the request is actually $30 million below fiscal year 1990 levels.

Programs for children fare even worse in the Administration's request. UNICEF is down $15 million or a decrease of 23 percent. Health accounts are down $7 million. Accounts to deal with AIDS are down $2 million. Population accounts are down $23 million. Child survival is up by $4 million and education us up by $3 million. Also, agricultural development, which has a long-term impact on children, is down by about $60 million.

A.I.D. is now putting development on a carrot and stick basis, setting aside $75 million for countries that accomplish policy reform.

During today's hearings we will explore where the missing links are for programs affecting children and refugees. First we will hear from a panel of witnesses with a wide range of experience, both in the field and in international organizations. After that we will hear from A.I.D. and the Department of State.

Again, let me say thank you to our distinguished panel, and to those who came in a bit late let me again apologize for our chairman, who is this morning quite ill and unable to be with us, but he does extend his apologies to you. Mr. Lehman and I will be happy to stand in, and hopefully others will be along as well.

At this point we will go to your prepared statements. Let me say first that we will include the entire statement in the record and if you can summarize that we will be very grateful. We will start with UNICEF, if we may. We will start with Kul Gautum—I hope I pronounced it correctly—who is the Director of Planning, and he is accompanied by Lawrence Bruce, who is the President of the U.S. Committee for UNICEF.

Mr. Gautum.

MR. GAUTUM'S OPENING STATEMENT

Mr. GAUTUM. Thank you, Mr. Chairman.

As you mentioned, we do have a prepared written statement for your records. I will speak to some of the points rather than reading from it.

Let me say also at the very outset that I am basically a field worker of UNICEF, having served for most of my career in developing countries, in Haiti, in Laos, Cambodia, Indonesia, my own country, Nepal. So if you find that my statement is not as refined as you are used to hearing, please forgive me.

We are grateful for this hearing, Mr. Chairman, on the needs of children and what might be some of the opportunities for action in the 1990's. We are particularly grateful because we know that at this time there are many other pressing issues demanding your attention. You have the need for support to the emerging new democracies in Europe and in Central America. You have the need for continuing support for your traditional allies in Asia and the Middle East. You have the needs with emergencies in Africa and you have the growing problems with debt, drugs, environment, et cetera.

When we see all of these major problems which are in the headlines of newspapers and television, we at UNICEF sometimes worry that the more mundane needs of children might be forgotten. And we are therefore all the more grateful to you that you have found it fitting to have this hearing specifically focusing on children.

CHILDREN'S NEEDS AND ISSUES

Mr. Chairman, for the children of the world the 1990's could be potentially the best of times, but also, if we are not careful, the worst of times. They could be potentially the best of times because of, I would say, three major developments.

One, the ending of the cold war is good news for children. We hope that with the end of the cold war more attention will be focused from the whole world on the real problems of people, including children.

Second, as you are aware, there have been some major dramatic developments in child survival and development in the 1980's, as a result of which millions of lives have been saved, and the same technologies for health, education, communication could be applied for a major advance for children in the 1990's.

A third hopeful sign is that we begin to see an increased political consciousness and commitment at the highest levels of leadership on the importance of investing in children. Perhaps the best expression of that is the forthcoming World Summit for Children in September 1990. For the children of the world there could not be a higher level forum than the World Summit to discuss their problems and issues, and we are very optimistic that the outcome of the summit will be a great blessing for the children of the world.

At the same time, as I was saying, if we are not careful potentially this could be the worst of times for children, and I say that, again, for three principal reasons.

One, in spite of all the progress that has been made, 40,000 children die every day in the world today, 14 million a year, and many of those deaths are because of fundamental underlying problems of poverty, ignorance, malnutrition. These problems are not easily going to go away, but are going to remain with us.

In the 1980's, as we are aware, many of these problems have worsened, particularly in Africa and in Latin America.

A second reason for concern is that, in addition to all of these problems that we have always had, in the 1990's we face some problems that were not very important in the 1980's. AIDS at the beginning of the eighties hardly existed. The problem of drugs has become much more serious. Debt has become worse. Environmental degradation has become worse. So in many ways, some of these problems are worsening.

And thirdly, I must say, while we all welcome the end of the cold war, there is in some circles a fear that attention might be diverted now to more domestic issues and other issues, rather than to problems of children in developing countries, if we are not careful. So because of that there could be some worsening of the situation of children.

Mr. Chairman, let me now dwell briefly on what are some of the major problems and needs, unmet needs, of children first, and then I would like to spend a few minutes discussing what are some possible opportunities for action. In terms of the major problems for children of the world, they are, when you really come down to it, the same problems that you and I and all of us would consider to be the problems of our own children.

Number one, survival. If they do not survive, everything else is meaningless.

Second, development, development to their full potential. That is what we all want for our children.

Third, the problem of protection in difficult times.

These I would say are the major problems. Let me give you some of the dimensions of these problems. First, taking survival, as I mentioned 40,000 children die every day, 14 million a year, and we know that the majority of these deaths are not because of some intractable problems that are very difficult to solve. Some of them are because of very simple kinds of diseases, against which there are readily preventable actions.

Out of the 14 million children dying, some four million die because of diarrhea; another three million or so die because of diseases that can be easily prevented with very low-cost immunizations. Another two million or so die because of pneumonia, which can be treated with very simple and low-cost antibiotics.

And there are children dying from malaria and a number of other diseases, but the majority of them are preventable through low-cost simple solutions that already exist.

On the question of the developmental needs of children, of course, development is ensured when children have educational opportunities, a healthy environment, economic opportunities, opportunities for political freedom and cultural participation. And on that score also, the children of the world face many serious unmet needs.

Let me just take two or three examples. In the education field, some 100 million children of primary school age in the world do not get to attend primary schools at present. Almost a billion adults in the world, most of them women, are illiterate, and in most of the developing countries there are no opportunities for early child development that gives a head start for a child's growth and development.

In the 1980's, Mr. Chairman, we have seen a major deterioration even in these meager educational services. There has been on the order of a 25 percent reduction in expenditures on education in the poorest countries. When you visit schools in Africa, many schools lack the barest minimum—no blackboards, no writing chalk, teachers not paid for many months, and problems of that nature.

This disinvestment in education undermines the foundation for the future development of many of these countries.

Finally, on the third aspect of the children's needs, the protection, protection in times of economic hardship or political violence is a major problem confronting children. Today some 20 percent of the world's children live in these especially difficult circumstances, whether they are refugees, they are orphans, abandoned, street children——

Mr. McHugh. Excuse me, what was the percentage?

Mr. Gautum. About 20 percent of the world's children.

And while the cold war is ending, there still are hot wars going on in some 25 to 30 countries in the world. And in today's warfare most of the victims, Mr. Chairman, are not soldiers; they are usually children and women. And some special measures for their protection are important.

REDUCING INFANT MORTALITY

I recite all of the statistics, not to depress us all, but also to say that, while these are real problems, in the 1990's we do have some glimmers of hope for some actions that can be taken. We believe that in the 1990's there is a real possibility for making major progress for children on a number of fronts.

First, with the available technologies and the communications power of the world, we believe that in the 1990's we could achieve almost a one-third reduction in infant and child mortality in the world. This could come to reducing the childhood deaths in the world from a level of around 150 million, 156 million, to 105 million, a 50 million reduction.

How would that be achieved? Through several interventions. The number one killer of children, diarrheal diseases, which killed four million children, last year we believe that those deaths could be halved in the 1990's; that the vaccine-preventable diseases which are responsible for some three million child deaths per year could be drastically reduced.

We believe that pneumonia, which is responsible for some two million child deaths, could be reduced. And there are a number of other major breakthroughs possible. Polio, a disease that cripples 200,000 children every year, could be eradicated from the face of the earth by the year 2000. Measles, which is the number one vaccine-preventable disease that kills one and a half million children, could be virtually eliminated by the end of the decade.

So there are all of these potentials available. What would it cost to do all of these things? That is always a challenging question. We are not sure. We do not have the final accounts, as it were. But we estimate that to make major progress in education, in health, in nutrition, water supply, some of the basic services for children, would perhaps require an investment of some $40 to $50 billion additional in developing countries, much of it coming from the resources of developing countries themselves.

But for the reduction of deaths, nearly two-thirds of the deaths that are caused by these three main killers—diarrheal diseases, vaccine-preventable diseases, and pneumonia, acute respiratory infection—we estimate that an additional $2 to $3 billion would be required to make a major dent that would help reduce child mortality by one-third in the 1990's.

Two to three billion dollars is a lot of money. However, everything being relative, it is also something like two percent of the poor developing countries' military expenditure a year. It is what the U.S. spends in cigarette advertising every year or what the Russians spend in the consumption of vodka every month. So that is the order of magnitude that we are really talking about.

But of course, money alone is not enough, Mr. Chairman. There are other things that are important. Infrastructures need to be built. Management systems need to be developed. Training needs to be provided. The communications technologies that are available today need to be harnessed.

COMMITMENT TO CHILDREN'S PROGRAMS

And all of this requires money, plus something else, and I would say that something else, the most important ingredient that is missing, is the political commitment, leadership, vision, and the will.

And from that point of view, again let me come back to the World Summit for Children. We do hope that this summit will make a major impact on that. We do hope that President Bush will attend the summit, bringing to the summit not only his own considerable authority, but also the strong backing and support of the Congress, the legislative branch of the government.

We are sure that there are many other heads of state who will be there looking to U.S. leadership. Therefore, the summit is something that we are really looking forward to as really making a major difference.

Mr. Chairman, I started my statement with a reference to the cold war and the hopeful signs coming from that. Let me end with another reference to an example from the cold war that we could emulate for doing a lot of good for children in the 1990's, in the post-cold war era.

In the 1950's and the 1960's, at the very height of the cold war, the U.S. and the U.S.S.R. showed a remarkable example of collaboration in the worldwide effort to eradicate smallpox, the first disease that was eradicated from Planet Earth through concerted human effort.

We would hope that, with the cold war ending and with the atmosphere of detente in the 1990's, that again these superpowers would join many other nations to spearhead a virtual revolution for child survival and development in the 1990's.

We at UNICEF have argued that such a major revolution for child survival and development is technically feasible, financially affordable, and that what really is lacking is the political leadership and commitment and vision. And I am sure you would agree, Mr. Chairman, that the cause of children, our common future, is certainly worth the highest priority for the leaders of the world to devote to it.

Thank you, Mr. Chairman.

Mr. McHugh. Thank you very much.

[The prepared statement of Mr. Gautum follows:]

unicef

United Nations Children's Fund

Statement of Kul C. Gautam
United Nations Children's Fund

before the

Foreign Operations Subcommittee
U.S. House of Representatives

March 27, 1990

Thank you, Mr. Chairman, for this opportunity to brief you and your colleagues during your important deliberations on the situation of the world's children, their unmet needs, and UNICEF's ideas and proposals for what can and needs to be done to meet these needs.

We are aware that your Committee has many other important matters demanding your attention. The newly emerging democracies of Eastern Europe and Central America have consumed the headlines in recent months. Then, there are the major global problems of debt, drugs and environmental degradation which also cry out for urgent attention.

In these times of such momentous change, we at UNICEF have feared that the more mundane needs of the world's children might be easily forgotten. After all children cannot vote,they do not protest, they do not have a loud enough voice to command the attention of the world's media. This is all the more reason why we are particularly grateful to you, Mr.Chairman, that you have found it fitting to devote this hearing to the needs of children.

For the children of the world, the 1990s could represent the best of times, but also possibly the worst of times. They could be the best of times because the end of the cold war could usher in a period of heightened attention to the real, serious problems of the world - among them the need to apply our present capacities to the pressing problems of children.

A series of rather recent breakthroughs in the fields of public health and communication also augur well for a major improvement in the situation of the world's children. We have seen in recent years, a growing awareness among the world's leaders that the future of their nations depends on investment in the well-being of their children.

An exciting example of this consciousness is the proposed World Summit for Children to be held at the United Nations in New York in September 1990. There is no higher level global forum to deal with the problems of children. It is our hope that this first ever World Summit on the needs of children and the solutions that exist to meet those needs will usher in a new era of commitment for vastly improving the situation of children.

Notwithstanding such possibilities for increased attention to the world's children, it is still possible that they could yet face the worst of times in the 1990s.

For instance, the heaviest burden of external debt and adjustment policies has fallen on the poor and vulnerable groups of developing countries, and disproportionately on women and children. Forty thousand children still die every day in developing countries. The new plagues of drugs, AIDS and environmental degradation threaten to make the situation worse in the coming years.

Thus unless deliberate action is taken, the promise of great improvement in the situation of children in the 1990s could turn into a continuing disaster of neglect. The challenge for all of us is how to make the 1990s a historic decade of hope and progress for the world's children.

Let me dwell on this challenge ahead by sharing with you first a picture of some of the most pressing needs of children and then some unprecedented opportunities for action that lie ahead.

At the most general level, the needs of the world's children are identical to what we all consider to be the most important needs of our own children. I would put these needs in three categories 1) survival, 2) development, and 3) protection.

1) The Survival Needs: These are, of course, the most basic of all needs. All other needs are meaningless, and secondary, if we cannot ensure survival. Survival is ensured by proper health care, adequate nutrition, protection against the elements and accidents.

Today some 14 million children under the age of five years die every year in developing countries. Figure 1 depicts the major causes of these deaths, many of which are attributable to multiple causes and therefore cannot be fully overcome by intervention against just the principal cause. However, the overwhelming majority of these deaths are preventable by health measures that are potentially within the reach of all communities.

At present less than 60 per cent of births in developing countries are attended by trained health personnel; about 500,000 women die each year from causes related to pregnancy and child birth, leaving over 1 million young children motherless; and less than half the married women of child-bearing age have the necessary knowledge to enable them to properly space child births and to prevent unwanted pregnancy.

In spite of much progress in recent years, one third of the world's children under one year of age are not fully immunized against the six vaccine-preventable diseases. Some 3 million children under five years old become seriously disabled each year from diseases that are preventable by immunization. Only about one third of the world's children are treated with oral rehydration salts, the most effective remedy against dehydration from diarrhoea, the single largest killer of children in developing countries.

About one third of all people in developing countries do not obtain sufficient energy to allow an active working life. About 40 per cent of children under five years old suffer from protein-energy malnutrition, and about 20 per cent of the infants in these countries are born with low birth weight (weighing less than 2.5 kilograms). Some 40 per cent of women of child-bearing age and half of the children under five years old suffer from nutritional anaemia. About 500,000 children under five years old lose their sight every year because of vitamin A deficiency. Within a few weeks of becoming blind, two thirds of those children die. Some 800 million people in the world are at risk of iodine deficiency disorders (IDD), of whom 200 million have actually developed goitre. Three million people - mostly children - suffer from cretinism, a debilitating disease that causes both mental and physical retardation.

The lack of adequate water and sanitation remains a problem for over a billion people in developing countries. Forty per cent of the children in these countries have no access to clean drinking water, while 75 per cent do not have adequate sanitation. In rural areas, the situation is much worse than these national averages.

2) Development Needs: These are what we all wish for our own children to grow to their full potential - education, a healthy environment, the opportunity to earn a decent living, political freedom and the ability to participate in cultural and spiritual pursuits.

Today, about 20 per cent of primary-school-age children in developing countries (about 100 million) do not attend school at all. Of those who attend, one third drop out of school before completing four grades. There are about 960 million illiterate adults in developing countries, two thirds of whom are women.

Pre-school child care services, so essential for a "head start" in early child development are virtually non-existent in most developing countries.

In the past decade spending on primary education has declined by 25 per cent in some of the poorest countries in the world. Most primary schools lack even the barest necessities such as blackboards, chalk and textbooks, and teachers are deserting the profession in droves as they are not paid their meagre salaries for months. In the face of such deterioration in basic education the very foundation for future development of many societies is severely undermined.

3) Protection Needs: Protection in times of economic hardship, political or social violence, natural disasters and societal neglect are another set of basic needs of children. Today children in especially difficult circumstances - as victims of armed conflicts, natural disasters and the breakdown of traditional family support mechanisms - account for some 20 per cent of children between the ages of 0-15 years old. The number of such children - be they abandoned street children, orphans, or those living in single-parent families - has been increasing, rather than diminishing in recent years. The world now has some 30 million refugees and displaced persons, a majority of whom are children.

The above are some of the most pressing physical problems of children. Overcoming those problems is essential for their survival, development and protection, but more is needed to enable them to lead lives with full human dignity and in ways that are culturally fulfilling, socially rewarding and intellectually stimulating. For this, children's needs extend to other areas of human endeavours that enable them to enjoy a quality of life that not only meets the bare necessities for survival, but allows them to develop to their full potential. As codified in the United Nations Convention on the Rights of the Child, it is hoped that these "needs" will truly be recognized as rights of children in the decade of the 1990s. We view this as not just a matter of society's obligation to a rising generation, but as an investment in the future development of the whole society.

Opportunities for Action

A decade or two ago, the world had only limited possibilities of effectively confronting many of the problems and needs of children. However, today, thanks to a series of technological breakthroughs and the communications revolution, it is quite conceivable to eradicate some of the most dreaded diseases, effectively prevent and treat many infections and disseminate the knowledge and skills for improving the quality of life of people heretofore unreached and unserved by the modern sector of the economy or government services.

For example, virtually all communities, even in the remote areas of developing countries, are now linked with metropolitan centres via radio and, increasingly, television, newspapers and video-cassette recorders (VCRs). Although actual use is still limited, basic education and health services are within reach of virtually all communities. The voices of religion, NGOs, commercial advertisements and official messages now reach unprecedented numbers of people. This capacity for communication, if combined with the low-cost, high-impact interventions in maternal and child health, water supply and sanitation, agriculture and nutrition, basic education and child development, is capable of producing a virtual revolution in the survival, development and protection of children.

The following are examples of some of the readily achievable actions that nations, working together, could pursue in the decade of the 1990s:

(a) The eradication of polio, which currently cripples an estimated 200,000 children a year;

(b) The elimination of iodine deficiency disorders, which cause severe mental and physical retardation in some 3 million people - mostly children - and affect 200 million people who suffer from goitre;

(c) The elimination of guinea worm disease (dracunculiasis), which currently afflicts and incapacitates 20 million people, mostly women and children in Africa;

(d) The elimination of neonatal tetanus, which kills over 750,000 children and many thousands of young women every year;

(e) The virtual elimination of measles - the largest singlevaccine-preventable disease - which kills 1.5 million children and exacerbates malnutrition among millions more every year;

(f) The virtual elimination of vitamin A deficiency, which totally blinds or impairs the eyesight of 500,000 children and contributes to the deaths of at least 100,000 more every year;

(g) A 50 per cent reduction in deaths caused by diarrhoeal diseases - the single largest killer of children in the world - which are responsible for 4 million child deaths every year;

(h) A 50 per cent reduction in deaths due to acute respiratory infections (ARI) - the second largest killer of children in most developing countries - which are responsible for some 3 million child deaths per year;

(i) A significant increase in educational opportunities for 100 million children and 960 million adults, most of them girls and women, who at present have no access to basic education and literacy;

(j) Access to clean drinking water and safe sanitation for over 1 billion people in the developing world who are presently deprived of these basic amenities.

The elimination or drastic reduction of diarrhoeal diseases, ARI and vaccine-preventable diseases alone, as per the above goals, could prevent some 50 million child deaths in the world in this decade, which would otherwise reach the tragic toll of 156 million deaths, if current rates prevail. These same measures, along with interventions to eliminate some of the micronutrient deficiencies, could prevent an equal number of children from being physically or mentally disabled.

Such a reduction in child deaths would help to set in motion an even greater reduction in the number of child births, as historical evidence indicates that a sustained decline in child mortality to a level where parents gain confidence in their capacity to ensure the survival of their first children is followed by even greater declines in fertility.

It has been estimated that, in addition to what the nations of the world are already investing in their development, an additional $50 billion per year - equivalent to 1 per cent of the world's combined annual gross national product (GNP), or 5 per cent of the world's annual military expenditure - might be required throughout the 1990s to meet the great human goals of adequate food, water, health care and education for all. However, the global price tag for the readily "do-able" health interventions that could reduce the world's child mortality by one third in the next decade, i.e. to prevent 50 million child deaths, would be in the range of $2 billion to $3 billion per year, which is roughly equivalent to the world military expenditure for just one day. Money alone, of course, is not enough.

Infrastructures need to be built, training needs to be provided, management skills need to be developed and all possible channels ofinformation, communication and education need to be mobilized to impartrelevant knowledge and skills to parents. All of this, however, is achievable given the most critical missing ingredients - the political will, vision and leadership.

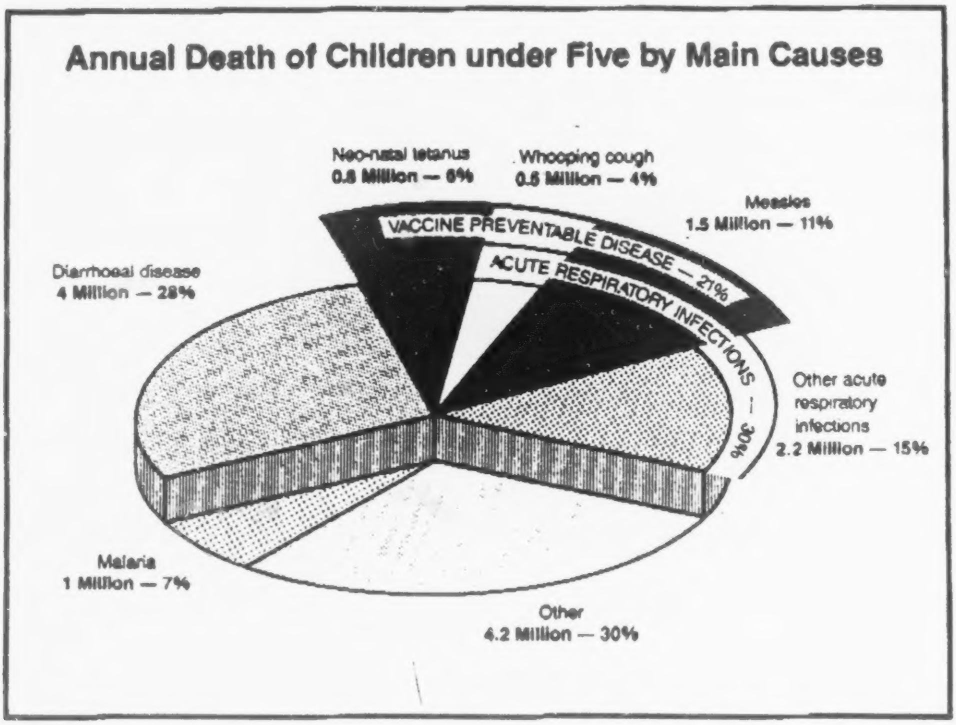
Speaking of political will, Mr. Chairman, the forthcoming World Summitfor Children is, of course, an expression of this will at the highest level of leadership. We at UNICEF are hoping that the United States will play an active role before, during, and after the Summit to forge a world-wide consensus for spearheading a virtual revolution in child survival and development. We would hope that President Bush will attend the Summit with not only the commitment of the Executive branch of the Government, but also with strong Congressional and public support for the well-being of the world's children.

As I began my testimony with a reference to the ending of the cold war and its hopeful consequences for children, may I close by referring to an extraordinary case of collaboration among the superpowers during the cold war which might now be emulated for even greater good of children in the post-cold war era.

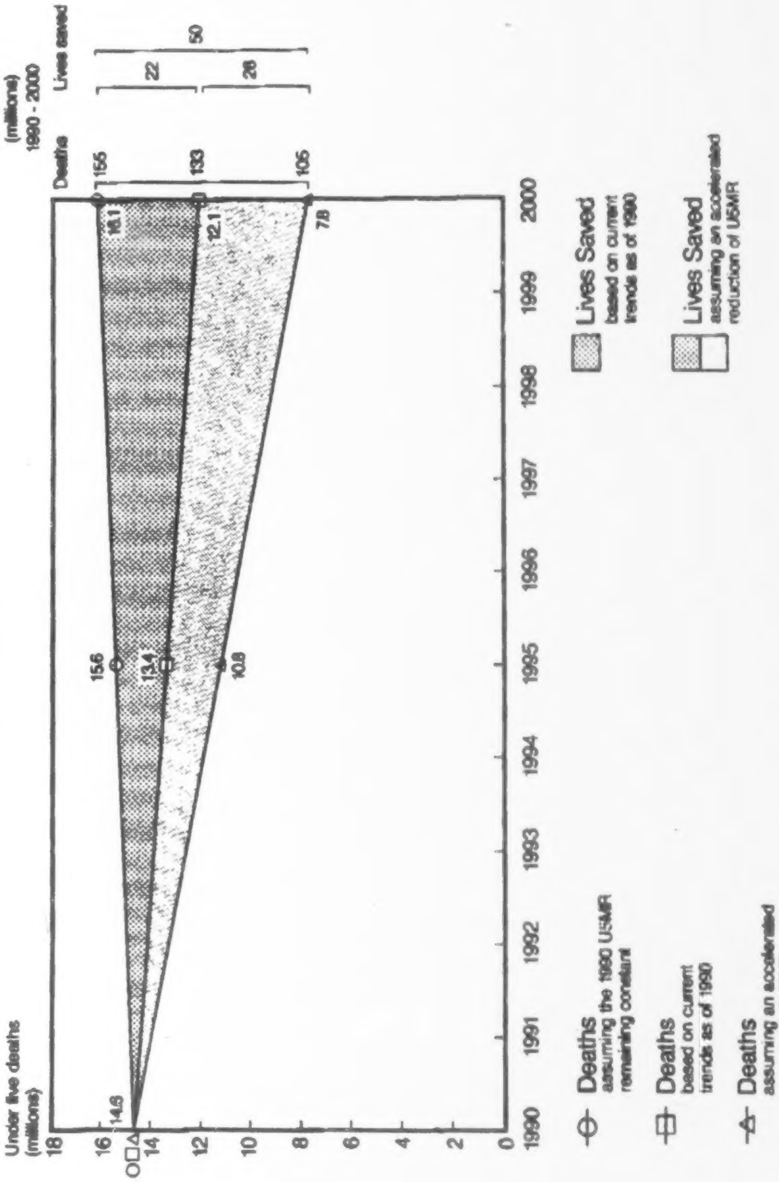
In the worst days of the cold war in the 1950s and 1960s the US and USSR gave a shining example of cooperation with other nations in the worldwide campaign to eradicate smallpox - the first disease eradicated from planet earth through deliberate human effort.

Would not it be most fitting, Mr. Chairman, that in the last decade of this century, and given the new atmosphere of detente - that the great powers join forces with other nations and organisations to spearhead a world revolution for child survival and development? As UNICEF has often argued, such a revolution is technically feasible, financially affordable and it is the best investment in our common future. Thank you, Mr. Chairman, I would be happy to answer your questions.

Figure 1


Annual Death of Children under Five by Main Causes
Neo-natal tetanus
0.8 Million — 6%
Whooping cough
0.6 Million — 4%
Measles
1.5 Million — 11%
VACCINE PREVENTABLE DISEASE — 21%
ACUTE RESPIRATORY INFECTIONS — 30%
Diarrhoeal disease
4 Million — 28%
Other acute
respiratory
infections
2.2 Million — 15%
Malaria
1 Million — 7%
Other
4.2 Million — 30%

ESTIMATED CHILD DEATHS AND LIVES SAVED 1990 - 2000



GOALS FOR CHILDREN AND DEVELOPMENT IN THE 1990s

The U.N. Convention on the Rights of the Child embodies the most comprehensive listing of goals for the well-being of children. Full implementation of the Convention is the ultimate objective of programmes for children and development. The following goals, derived through a process of extensive international consultation, are essential means to achieve that ultimate objective.

I. Major Goals for Child Survival, Development and Protection

- Between 1990 and the year 2000, reduction of infant and under-5 child mortality rate in all countries by one-third or to 50 and 70 per 1000 live births respectively, whichever is less.
- Between 1990 and the year 2000, reduction of maternal mortality rate by half.
- Between 1990 and the year 2000, reduction of severe and moderate malnutrition among under-5 children by half.
- Universal access to safe drinking water and to sanitary means of excreta disposal.
- By the year 2000, universal access to basic education and completion of primary education by at least 80% of primary school age children.
- Reduction of the adult illiteracy rate (the appropriate age group to be determined in each country) to at least half its 1990 level with emphasis on female literacy.
- Improved protection of children in especially difficult circumstances.

II. Supporting/Sectoral Goals

1. *Women's Health and Education*

- Special attention to the health and nutrition of the female child, and pregnant and lactating women.
- Access by all couples to information and services to prevent pregnancies which are too early, too closely spaced, too late or too many.
- Access by all pregnant women to prenatal care, trained attendants during child birth and referral facilities for high risk pregnancies and obstetric emergencies.
- Universal access to primary education with special emphasis for girls, and accelerated literacy programmes for women.

2. *Nutrition*

- Reduction in severe as well as moderate malnutrition among under-5 children by half of 1990 levels.
- Reduction of the rate of low birth weight (2.5 kg or less) to less than 10%.
- Reduction of iron deficiency anaemia in women by one-third of 1990 levels.
- Virtual elimination of iodine deficiency disorders.
- Virtual elimination of vitamin A deficiency and its consequences, including blindness.
- Empowerment of all women to exclusively breast-feed their child for four to six months and to continue breast-feeding with complementary food well into the second year.
- Growth promotion and its regular monitoring to be institutionalised in all countries by the end of the 1990s.
- Dissemination of knowledge and supporting services to increase food production to ensure household food security.

3. *Child Health*

- Global eradication of poliomyelitis by the year 2000.
- Elimination of neonatal tetanus by 1995.
- Reduction by 95 percent in measles deaths and reduction by 90 per cent of measles cases compared to pre-immunisation levels by 1995, as a major step to the global eradication of measles in the longer run.
- Maintenance of a high level of immunisation coverage (at least 85% of children under one year of age) against diphtheria, pertussis, tetanus, measles, poliomyelitis, tuberculosis and against tetanus for women of child bearing age.
- Reduction by 50 per cent in the deaths due to diarrhoea in children under the age of five years; and 25 per cent reduction in the diarrhoea incidence rate.
- Reduction by one-third in the deaths due to acute respiratory infections in children under five years.

4. *Water and Sanitation*

- Universal access to safe drinking water.
- Universal access to sanitary means of excreta disposal.
- Elimination of guinea-worm disease (dracunculiasis) by the year 2000.

5. *Basic Education*

- Expansion of early childhood development activities including appropriate low-cost family and community based interventions.
- Universal access to basic education, and achievement of primary education by at least 80 per cent of primary school age children through formal schooling or non-formal education of comparable learning standard, with emphasis on reducing the current disparities between boys and girls.
- Reduction of the adult illiteracy rate (the appropriate age group to be determined in each country) to at least half its 1990 level, with emphasis on female literacy.
- Increased acquisition by individuals and families of the knowledge, skills and values required for better living, made available through all educational channels, including the mass media, other forms of modern and traditional communication, and social action, with effectiveness measured in terms of behavioural change.

6. *Children in Difficult Circumstances*

- Provide improved protection of children in especially difficult circumstances and tackle the root causes leading to such situations.

Mr. McHugh. Mr. Bruce, would you like to add to that as the spokesperson for the U.S. Committee?

Mr. Bruce's Opening Statement

Mr. Bruce. Yes, I would. Mr. Chairman, it is a pleasure to see you, to be with you again, and I want to thank you and to let you know that I am here representing thousands of volunteers of the United States Committee for UNICEF across the country, as well as our board of directors and our staff. And we are quite appreciative for the opportunity to present the perspective of many American people regarding the state of the world's children and the role the United States can and should play in addressing these needs.

I bring to this committee warm greetings from the chair of our board, Hugh Downs, who has testified here a number of times, and he too is extremely pleased to learn that the chairman of this committee continues to place children's issues toward the top of the committee's agenda.

As you are aware, the American people also continue to be strong supporters of UNICEF. I mentioned that we have thousands of volunteers. They are in all 50 States, as well as our contributors. Last year, private individuals and corporations contributed $16 million directly toward the adoption of UNICEF-assisted projects.

As you know, Mr. Chairman, UNICEF does not get a slice of the United Nations pie. Every year UNICEF must go out and raise the contributions toward the UNICEF budget. These are voluntary contributions, both governmental and private.

On the private side of this, for many years about 25 percent of UNICEF's budget is derived from private sources, primarily from the 34 national committees that exist in industrialized countries. I also serve as the global chairman of these 34 national committees.

UNICEF, as you have heard, continues to be an organization working on behalf of certainly the most vulnerable and the most poor in 121 developing countries. This work is clearly heartily supported by the grassroots here in the United States.

However, while we are doing our best within the United States Committee for UNICEF to increase our level of support each year, the task at hand, as you mentioned yourself, Mr. Chairman, and as you heard from Mr. Gautum, during the 1990's is enormous.

The goal clearly is to save and to improve the lives of 50 million children over the course of the next decade, and this is up against the tremendous problems, as you well know, of debt and global recession. This goal of saving at least 50 percent of the over 150 million of the world's children now destined to die in the 1990's from largely preventable diseases may seem somewhat remote and may seem somewhat difficult.

But clearly we know that the need is there. We know what is happening. We have the means to prevent this, and it is unconscionable for us to stand back and allow 150 million children to die of preventable causes during the 1990's.

While this might seem a rather rigorous task, I would remind the committee of what is happening on universal child immunization. When this was announced at the beginning of the eighties, it seemed as if to immunize the world's children was almost an im-possibility. Only about ten percent of the world's children were immunized at that point.

But now we are within reach in the majority of the developing countries to show that this can be done. UNICEF and WHO now report that the immunization rate during the decade of the eighties has now climbed to 70 percent. This means that 70 percent of the world's children are protected against the six killer diseases.

We are almost there, but it is clearly going to be a stretch to try and complete this work by the end of 1990, which is the goal.

UNICEF and its partners, including U.S. AID, Save the Children, and others represented here who have collaborated on child survival activities, have shown that a great deal can be done with relatively little money. This is clear if societies mobilize on behalf of their own children.

We have seen this with immunization. We have seen it, as you have heard from Mr. Gautum, on oral rehydration therapy. And we feel that it clearly can be repeated throughout the nineties.

However, it will require increased funding. And UNICEF can put every dollar it gets from us within the U.S. Committee, as well as the Congress, to good use toward these goals.

UNICEF PROJECTS

I want to assure the members of this committee that the United States Committee for UNICEF does not just accept in blind faith what UNICEF is doing. As President and CEO of this organization, I have traveled to visit UNICEF-assisted projects on every continent.

I have just returned very recently, just days ago, from Bangladesh. It is the second largest program that UNICEF has, next to India, and there I saw sanitation and water improvement projects throughout the slums of Dacca, in a village, Balucca. I visited experimental schools where they have been able to, with UNICEF assistance, increase the attendance of children in schools from 25 percent to 85 percent. I saw immunization projects throughout Balucca.

Going on to a city by the name of Maimensing, I saw slum improvement projects. I saw women income-generating projects. And time and time again, I am touched by what I mentioned earlier, how little money it takes to make an extreme difference in people's lives.

Just a few months ago I took a delegation of members of my board to Guatemala and Honduras, and I will just give you hopefully a 60-second example of one small village with about 30 families that we visited in the very southernmost part of Honduras.

UNICEF helped support a little baking operation there, where the women made a type of empanadas in one of the homes, which they carried to a larger city for sale. They were then able to build a supply storehouse with the profit. UNICEF assisted with some of these supplies.

From these meager beginnings, they made additional funds and built a pre-school, not what we would think in this country of a pre-school. It is some rather large limbs with a roof. But again, it was the first opportunity that the children in this community had ever had for education.

From the Hurricane Gilbert that devastated so much of that country, this community was also trying to restore the houses that were destroyed, basically mud and sticks.

This entire project, all of these various pieces, were done with less than $50 of UNICEF assistance. To see the difference that it made in these people's lives, it was so real you could literally reach out and touch it. And as well as educating the children, the women were being educated in child survival techniques, such as immunization and ORT and others. So again, it is just the sense that so much can be done with so little.

U.S. CONTRIBUTION TO UNICEF

I would like to also mention, if I might, a few words about the United States voluntary contribution to UNICEF. We are pleased that the Administration's request is considerably higher than recent years. However, it is still, as you mentioned, Mr. Chairman, approximately 23 percent below the fiscal year 1990 level of our appropriation. As such, this is clearly not supported by the American constituency for UNICEF.

I would like to clearly praise this committee in particular and the chairman that leads this committee for rescuing the UNICEF contribution over these past few years and for shepherding through the Congress increases for UNICEF. And these increases have encouraged other nations to follow the lead of the United States and to make higher contributions of their own.

I would conclude my remarks, Mr. Chairman, by urging that the United States stay in the forefront of UNICEF's and other's child survival and development programs for the 1990's, and I would also request on behalf of our constituency that the appropriation for UNICEF be increased to $75 million.

Thank you very much.

Mr. McHugh. Thank you very much, Mr. Bruce.

Our next presenter will be Ms. Phyllis Dobyns, who is Senior Vice President of Save the Children.

Ms. Dobyns' Opening Statement

Ms. Dobyns. Thank you very much, Mr. Chairman and committee members. I really am grateful to all of you for holding this committee hearing. It really gives us an opportunity to share with you some of the things we see in the field all the time impacting on children.

I am really honored to have with me one of my colleagues who has been a hero for children out in Mozambique, and he will speak to you about one of the worst travesties impacting on children today. But I would like to first try to present a broader, global picture of a situation that I feel is impacting terribly on children, particularly refugee children.

REFUGEE CHILDREN

The 1990's will be known as the decade of the refugee. Now numbering nearly 15 million around the globe, their ranks are expected to swell in the years ahead. In quiet despair they will continue their flight from violence and oppression in search of a safe haven, wherever that may be.

In the past two years alone, their numbers have increased by seven million, as conflict and unrest have swept through Africa, Asia, Central America, and Eastern Europe. The hardship and suffering that they endure will continue, but the most tragic victims of the nineties will be the children. It has been estimated that up to 40 percent of all refugees are children under the age of five, and every day more babies are born within the confines of refugee camps.

In temporary settlements in Zimbabwe, in detention centers in Hong Kong, and in sprawling tent cities in Pakistan, a generation of children are now approaching adulthood with no experience other than that of the camps. Literally hundreds of thousands while away years without productive activity and, most importantly, without the opportunity to learn.

Despite the widespread recognition by the international community that education is a basic right, most refugee children do not have access to even primary education. The reasons for this are varied. Insufficient national resources, coupled with declining funds for the United Nations High Commissioner for Refugees, and the lack of both teachers and teaching materials in appropriate languages are perhaps the chief among them.

In 1987, the last year for which reliable data regarding education is available from the UNHCR field offices, 463,000 refugee children benefited from educational assistance. That is good, but it is not enough.

Even if the number of children reached had doubled in this past two years, it would still mean that as many as 85 percent of all refugee children are not being educated. This threatens an entire generation of potentially productive citizens. If we do not provide these children with even the most basic educational foundation on which they can build fruitful lives, we are not only diminishing, even destroying, their potential; we are guilty of the worst kind of neglect.

Who are these refugee children? These are more than faceless numbers. The wonder of children is that they are human beings so full of potential that it is impossible to predict who they may become and what they may contribute to society and to the world.

That they have been uprooted and relegated to the humiliating status of refugee does not lessen their inherent promise. Consider Frederick Chopin, Albert Einstein, and Sigmund Freud, all refugees in earlier times.

The difference in the refugee experience of the nineties is that for so many children it is an existence that seems never to end. Its ceaseless monotony of deprivation and indignity shapes the child's identity, sometimes in irreparable ways.

Perhaps it was simpler when the numbers were smaller. Humanitarian aid seemed to stretch further then. Today the need far outpaces the human and financial resources dedicated to the task of caring for people seeking refuge.

As the demands upon the United Nations High Commissioner for Refugees have expanded, private voluntary organizations have stepped in. With their characteristic flexibility and people to people approach, they have been singularly effective in engaging refugees themselves in rebuilding the fabric of their lives.

There is more to humanitarian aid than filling empty bellies and building shelters. Ensuring that children receive the minimal nutritional requirements which are essential for the development of both their bodies and their minds is a need certainly of equal measure.

Fulfilling that need while keeping the human spirit alive in the midst of what for many is a dehumanizing experience is what private voluntary organizations do so well. Studies have shown that when refugees are subjected to handouts day after day they come to believe they cannot provide for themselves. Children learn from their parents and soon contract the same disease of dependency.

SAVE THE CHILDREN PROJECTS

Save the Children is working with more than 750,000 Mozambiquans in Malawi, Zambia, and Zimbabwe. Our approach goes beyond meeting the basic refugee needs. First, the active involvement of the refugee is key, because dependency and depression become the immediate and lasting result when refugees are not encouraged or allowed to make decisions about their own lives. So participation is the first step in our projects.

In our early childhood education project, for example, parents either help build a pre-school classroom or pay a small fee so their children can attend. And while children are being taught basic learning skills, parents are trained in carpentry, auto mechanics, and other transferable job skills that will enable them to earn income to support their families when they return home.

In Zimbabwe's Tongongara refugee camp, a children's agricultural project is answering another important problem facing refugee children. In a refugee camp children are cut off from the rich learning experiences of village life. For example, if the children were living in their villages they would be helping their parents farm and herd the animals. In the camp, they are deprived of this opportunity, and without learning skills that are basic to their world they will be unskilled, unprepared, and unproductive when they resume their village lives.

Perhaps the best example of the value of a PVO initiative and involvement can be found in Asia. Against a backdrop of some of the worst human rights violations in the world, private voluntary organizations are working hand in hand with the UNHCR to lessen the suffering among refugees and asylum-seekers.

In Galang, Indonesia, and Phanat Nikhom, Thailand, World Education, the Experiment in International Living, and Save the Children have worked in consortium with funding from the U.S. State Department Bureau of Refugee Programs to create a uniquely effective cultural orientation and training program for Indochinese families awaiting resettlement in third world countries.

The investment in such programs more than pays off. Take Quang Pham for example. After surviving a terrifying trip by sea as one of the boat people to Galang, Indonesia, Quang Pham was able to take advantage of primary school and later the secondary education program. In the two years he was awaiting resettlement, he worked hard and learned a great deal.

Later, in Bridgeport, Connecticut, Quang Pham attended an inner city school. Again he did well, eventually winning a scholarship from a local fraternity organization. Today Quang Pham is an honors student at the University of Connecticut.

Despite the successes of the education programs and of individuals like Quang Pham, concern among program staff and refugees alike is mounting. There are more unaccompanied children than ever before. Already today in Galang there are 350 of these solitary youngsters among asylum seekers. Currently there are no programs that reach out to them.

And now the sailing season has begun and the influx of new families seeking asylum is on the rise. Yet the pace of the screening process is so slow that it threatens to entrap thousands of youngsters in the camps for five, maybe ten years. The implications of this situation are profound.

These children may be resettled, with or without their parents, repatriated, voluntarily or forcibly. But the issue remains. Children have a right to a childhood.

The denial of basic human rights to refugee children the world over presents one of the most dramatic cases for speedy ratification of the International Convention on the Rights of the Child. Article 22 of the convention specifically grants special protection to children who are refugees or seeking refugee status and sets forth the state's obligation to cooperate with competent organizations providing such protection and assistance.

These good intentions must be translated into reality. Protecting and nurturing refugee children is a responsibility that belongs to each and every one of us. Humanitarian assistance to refugees in all its forms is a sound investment. This holds true in faraway countries, but also right here in the United States, where the ingenuity, resources, and passionate loyalty of former refugees contributes greatly to our national strength today and in the years to come.

SAVE THE CHILDREN RECOMMENDATIONS FOR THE COMMITTEE

Mr. Chairman and committee, we strongly recommend the following:

That the funding appropriated for the vital work of the United Nations High Commissioner for Refugees be increased;

In particular, that the importance of early nutritional and preventive health programs, as well as adequate educational programs for refugee children, be recognized through appropriate funding for the UNHCR and the World Food Program and through adequate monitoring of programs;

That Congress request the UNHCR to report annually by country and by gender the total proportion and number of children, refugee children, attending primary school and the number of refugee minors in vocational or skills training programs;.

And finally, I really urge you to get the Congress to work toward the ratification and implementation of the International Convention on the Rights of the Child. In doing so, Congress will send a clear message to all other nations that the United States recognizes that humanitarian aid encompasses the right of every refugee adult and child to retain human dignity, to have equal access to health care and education, and to the opportunity to develop untapped potential.

To do less is to deprive the world of a valuable gift. Perhaps Nobel Laureate Elie Weisel put it best: "In times of crisis and human tragedy, ignorance is complicity and silence is a crime."

Thank you.

Mr. Chairman, I would also like to mention that, in terms of some of the facts I have for refugees being assisted overseas, I found it astounding to find that in 1984 the per capita dollars spent, budgeted for refugees, was $20. In 1989 it is $11, and any one of us here can certainly understand that $11 to aid a refugee for a year is unrealistic in terms of trying to meet even the most basic human needs.

I urge you to consider our recommendations, and I am honored to have with me a man from the field who has become a real hero for children by breaking the silence of the travesty impacting our children in Mozambique. Thank you.

Mr. McHugh. Thank you very much.

[The prepared statement of Ms. Dobyns follows:]

TESTIMONY OF

PHYLLIS DOBYNS
SENIOR VICE PRESIDENT
SAVE THE CHILDREN

BEFORE THE HOUSE COMMITTEE ON APPROPRIATIONS
SUB-COMMITTEE ON FOREIGN OPERATIONS, EXPORT FINANCING
AND RELATED PROGRAMS

MARCH 27, 1990

WHAT PRICE, REFUGEE CHILDREN?

Mr. Chairman:

Thank you for this opportunity to speak on behalf of refugee children around the world.

The 1990s will be known as the decade of the refugee. Now numbering nearly 15 million around the globe, their ranks are expected to swell in the years ahead. In quiet despair they will continue their flight from violence and oppression in search of safe haven -- wherever that may lead. In the past two years alone, their numbers have increased by 7 million, as conflict and unrest have swept through Africa, Asia and Central America and now Eastern Europe. The hardship and suffering they have endured will continue, but the most tragic victims of the 90s will be the children. It has been estimated that up to 40 percent of all refugees are children under the age of five. And every day more babies are born within the confines of refugee camps.

In temporary settlements in Zimbabwe, in detention centers in Hong Kong and in sprawling tent cities in Pakistan, a generation of children is now approaching adulthood with no experience other than that of the camps. Literally hundreds of thousands while away years without productive activity, and most importantly, without the opportunity to learn.

Despite the widespread recognition by the international community, including the executive committee of UNHCR, that education is a basic right, there are refugee children who do not have access even to primary education. The reasons for this are varied. Insufficient national resources coupled with limited UNHCR funds and the lack of both teachers and teaching materials in appropriate languages are perhaps chief among them. In 1987, the last year for which reliable data regarding education is available from UNHCR field offices, more than 463,000 refugee children benefitted from educational assistance. That is good, but it's not enough. Even if the number of children reached had doubled in the two years that have passed, it would still mean that as many as 85 percent of all refugee children are NOT being educated. These children are the forgotten casualties of our inability to deal effectively with the complex political, social and economic issues surrounding this growing tide of humanity.

That inability, moreover, threatens an entire generation of potentially productive citizens. If we do not provide these children with even the most basic educational foundation on which they can build fruitful lives, we are not only diminishing, even destroying, their potential, we are guilty of the worst kind of neglect.

Who are these refugee children? They are more than faceless numbers. The wonder of children is that they are human beings so full of potential that it is impossible to predict who they may become, and what they may contribute to society and to the world. That they have been been uprooted and relegated to the humiliating status of refugee does not lessen their inherent promise. Consider Frederick Chopin, Albert Einstein and Sigmund Freud -- all refugees in an earlier time.

The difference in the refugee experience of the 90's is that for so many children, it is an existence that seems never to end. Its ceaseless monotony of deprivation and indignity shapes the child's identity, sometimes in irreparable ways. Perhaps it was simpler when the numbers were smaller. Humanitarian aid seemed to stretch further then. Today the need far outpaces the human and financial resources dedicated to the task of caring for people seeking refuge.

As the demands upon the United Nations High Commissioner for Refugees have expanded, the non-governmental organizations have stepped in. With their characteristic flexibility and people-to-people approach, they have been singularly effective in engaging refugees themselves in rebuilding the fabric of their lives.

There is more to humanitarian aid than filling empty bellies and building shelters, important as those functions may be. Ensuring that children receive the minimal nutritional requirements which are essential for the development of both their bodies and minds is a need certainly of equal measure. Fulfilling that need, while keeping the human spirit alive in the midst of what for many is a dehumanizing experience is what private voluntary organizations do so well. Studies have shown that when refugees are subjected to hand-outs, day after day, they come to believe they cannot provide for themselves. Children learn from their parents and soon contract the same disease of dependency. Even more than their parents, children need help in coping not only with the terrors that propelled them into flight, but also with the difficulties -- even dangers -- of camp life itself.

In the meantime, people continue on the move throughout the world. In Southern Africa, for example, RENAMO has been at war with the Mozambican government since 1974. As the struggle drags on, the rebels have resorted to increasingly vicious acts of terrorism -- particularly in the countryside -- which have forced more and more people from their homes and villages. More than 2 million of Mozambique's 17.5 million people have sought refuge in other parts of Mozambique or in neighboring countries.

The number of Mozambican refugees in surrounding countries -- countries, it should be noted that are among the most fragile economically -- has been increasing dramatically. Last year, the population of Ukwimi, a settlement in Zambia, grew from 4,000 to 18,000 refugees. An essential water point near a camp in Malawi that was built to serve 250 people is now used by at least 1,000 -- and Mozambicans are seeking refuge in Malawi at a rate of more than 100 a day.

Save the Children is working with more than 750,000 Mozambicans in Malawi, Zambia and Zimbabwe. Our approach goes beyond meeting the refugees' basic -- and very important -- needs. First, the active involvement of refugees is key because dependency and depression become the immediate and lasting result when refugees are not encouraged -- or allowed -- to make decisions about their own lives. So participation is always the first step in our projects. In our early childhood education projects, for example, parents either help to build pre-school classrooms or pay a small fee so their children can attend. And while children are being taught basic learning skills -- in Portuguese, the official language of their country -- parents are trained in new carpentry, auto mechanics metalwork and other transferable job skills that will enable them to earn income to support their families when they return home.

The Children's Agricultural Project in Zimbabwe's Tongongara Refugee Camp is answering another important problem facing refugee children. In a refugee camp children are cut off from the rich learning experiences of village life. For example, if the children were living in their villages, they would be helping their parents farm and herd animals. In the camp, they are deprived of this opportunity. And without learning skills that are basic to their world, they will be unskilled, unprepared and unproductive when they resume their lives.

In fact, as Save the Children discovered, most of Tongongara's children under the age of eight didn't know the difference between a dog and a goat, or where milk comes from, or any of the simple facts of everyday life in any Mozambican village. To ensure that the vital cultural and economic link is not broken, Save the Children has introduced its own village farm, right in the camp. Each day 300 children come in the morning and 300 more in the afternoon, to learn to feed and care for goats, cows, chickens, ducks, pigs, geese and rabbits. They also grow cabbage, onions, tomatoes, carrots, spinach and rape. One-third of the crops and livestock is shared among the child farmers and the rest is sold to produce revenue for reinvestment in the farm.

Another aspect of refugee programs in Africa and throughout the world is addressing the needs of local communities. Frequently, tensions arise when nearby villagers see refugee camps with services -- schools, preventive health care, water sources -- that they never had. Nongovernmental organizations play a critical role in assuring that the needs of villages as well as refugees are met. The services provided in camps by UNHCR, for example, can be emulated -- by local, national and international NGOs -- in surrounding villages. This reduces the understandable tension between the "host" population and refugees.

The mobility and responsiveness of nongovernmental organizations has also been integral to UNHCR's education efforts around the world. Once again, NGOs can train teachers among the refugees and establish classes, providing training and employment for refugees as teachers as well as the necessary learning for children. Without this input of resources, infrastructure is simply not enough. The cost of inadequate education is the normal intellectual and social development of thousands of children. That is a cost that we all must agree is unacceptable.

Perhaps the best example of the value of NGO initiative and involvement can be found in Asia. Against a backdrop of some of the worst human rights violations in the world, non-governmental organizations are working hand-in-hand with UNHCR to lessen the suffering among refugees and asylum seekers. In Galang, Indonesia, and Phanat Nikhom, Thailand, World Education, the Experiment in international Living and Save the Children have worked in consortium with funding from the U.S. State Department Bureau of Refugee Programs to create a uniquely effective cultural orientation and training program for Indochinese families awaiting resettlement in third countries.

In Thailand, the Consortium's PASS program prepares Indochinese refugee teenagers to meet the academic and social challenges of the American high school. In addition, Save the Children's Child Care Center provides supervised child care and operates an early childhood education program for children between the ages of 6 months and 6 years. For children between age 6 and 13, Save the Children runs a primary school where English, mathematics and native language are taught to more than 1,000 refugee children each day.

In Indonesia, where, unlike in Thailand, it is possible to work with Vietnamese asylum seekers whose refugee status has not yet been determined, Save the Children has provided primary education to more than 90 percent of the camp's children between the ages of 5 and 8. In addition the secondary education program has reached more than 90 percent of refugees between the ages of 9 and 15.

The investment in such programs more than pays off. Take Quang Pham for example. After surviving a terrifying trip by sea to Galang, Indonesia, Quang Pham was able to take advantage of primary school, and later the secondary education program. In the two years he was awaiting resettlement in the United States he worked hard and learned a great deal.

Later, in Bridgeport, Connecticut, Quang Pham attended an inner city school. Again, he did well, eventually winning a scholarship from a local fraternal organization. Today Quang Pham is an honors student at the University of Connecticut.

Despite the successes of the education programs and of individuals like Quang Pham, concern among program staff and refugees alike is mounting. There are more unaccompanied children than ever before. Already in Galang, there are 350 of these solitary youngsters among asylum seekers. Currently, there are no programs that reach out to them. And now the "sailing season" has begun and the influx of new families seeking asylum is on the rise. Yet the pace of the screening process is so slow that it threatens to entrap thousands of children in the camps for five to 10 years or more. The implications of this situation are profound.

In the meantime, the detention camps in Hong Kong hold the headlines as additional horrors unfold. Perhaps none is greater than that of a child born to a world of concrete and barbed wire, a child who passes through the precious childhood years without ever seeing grass, unaware that there is color and shape and texture in a world outside.

These children may be resettled, with or without their parents, repatriated, voluntarily or forceably, but the issue remains. Children have a right to a childhood. The denial of basic human rights to refugee children the world over presents one of the most dramatic cases for speedy ratification of the international Convention on the Rights of the Child. Article 22 of the Convention specifically grants special protection to children who are refugees or seeking refugee status, and sets forth the State's obligation to cooperate with competent organizations providing such protection and assistance. But mere words on paper are not enough. These good intentions must be translated into reality. Protecting and nurturing refugee children is a responsibility that belongs to each and every one of us.

Humanitarian assistance to refugees in all its forms is a sound investment. This holds true in faraway countries, but also right here in the United States where the ingenuity, resources and passionate loyalty of former refugees contributes greatly to our national strength today and in the years to come.

We strongly recommend the following:

0 That Congress work toward the ratification and implementation of the international Convention on the Rights of the Child.

0 That the funding appropriated for the vital work of the United Nations High Commissioner for Refugees be increased. In particular:

--That the importance of early nutritional and preventive health programs as well as adequate educational programs for refugee children be recognized through appropriate funding for UNHCR and the World Food Program and through adequate monitoring of programs.

-- That Congress requests UNHCR to report annually, by country, and by gender, the total proportion and number of refugee children attending primary school and the number of refugee minors in vocational or skills training programs.

0 That more funds be made available for the complementary rehabilitative work of non-governmental organizations.

In doing so, Congress will send a clear message to all other nations that the United States recognizes that humanitarian aid encompasses the right of every refugee adult and child to retain human dignity, to have equal access to health care, to education and to the opportunity to develop untapped potential.

To do less is to deprive the world of a valuable gift.

Perhaps Nobel Laureate Elie Weisel put it best:

"In times of crisis and human tragedy, ignorance is complicity and silence is a crime."

Mr. McHugh. Dr. Boothby.

Dr. Boothby's Opening Statement

Dr. Boothby. Thank you very much, Mr. Chairman. And I also want to thank members of the committee for inviting me here and acknowledge the committee's strong leadership in this area.

Colleagues to the left and I am assuming colleagues to the right will continue to talk about the need for more funding for children in these war and refugee crises, and I certainly want to lend my support to that notion as well.

I think what I would like to do, though, at this moment is talk a little bit about what we do with this money and raise the question perhaps of whether we can think of better ways to utilize it. I think that the need is great. We have also heard that from various members here, and I think until we reach a point where we learn to prevent war that the international community is going to want to do all it can do to empower families and communities and nations to protect their children from the effects of war in particular.

Not only is this an international humanitarian imperative, but it probably is one of the few available strategies that we possess to begin to stop some of the inter-generational transmission of violence that leads to terrorism in many parts of the world and other kinds of problems that we face today.

We have some good international legislation in this area, most recently the Convention on the Rights of the Child, as well as earlier, equally important legislation. The question I think is, do we have the knowledge and the wherewithal to implement this legislation and to protect children in these circumstances. This is the main question that we attempted to address several years ago when we initiated a study on this subject that was funded by the UNHCR and UNICEF and other organizations that work in this area, as well as foundations such as Ford.

What we found in general was that within the international community there are some very good, coherent and strong policies and programs in the area of primary health care and nutrition. However, when it comes to protecting children's psychosocial needs in war and refugee situations, there are very few agencies that have coherent, sound policies and programs.

In fact, we have found that in many instances some misguided efforts by agencies actually caused some of the problems that they were trying to alleviate. In particular, one of the main findings was that over half of the separations that occur in war situations are not the result of parental death, but are preventable, mostly due to poverty, and other social, economic, and cultural factors.

Yet, very few agencies have policies that address this particular phenomenon. In some cases, when agencies, for example, rely on orphanages or children's centers and initiate other kinds of centralizing activities in the midst of a crisis, such actions actually act as magnets that pull children out of their families and in fact cause separations.

We found as well that preferential resettlement status given to unattached children also causes families to voluntarily give up their children, as does international adoption, for example, in war and refugee crises. It tends to undermine the community's own ability to take care of its children.

MOZAMBIQUE RELIEF EFFORT

On the other hand Mozambique is an example of a relief effort that has worked relatively well. The program was initiated in 1988 by the Office of Foreign Disaster Assistance and Save the Children and myself. It was funded, I think I am correct, through funding that was earmarked by this committee for orphans and unaccompanied children. I think in some ways it is an example of the kind of organizational support, funding support, and perhaps child care expertise that needs to come together if we are going to develop more coherent responses in these areas.

Essentially what we have attempted to do in Mozambique is work with the Ministry of Health, the Ministry of Education, the women's organization, and other groups within Mozambique to train personnel to begin to respond in very simple ways to some of the psychosocial needs of children in that country.

Now, this is a country that has been devastated by war for over 15 years, and official estimates suggest that perhaps 500,000 children have witnessed their parents and other family members killed, and perhaps somewhere in the neighborhood of 200,000 children have been separated from their families.

In training Mozambican people throughout the course of the last year and a half—and about 500 Mozambicans have been trained now—we have implemented strategies and basic techniques to begin to try to prevent separations, to begin to treat in culturally appropriate ways some of the traumatic experiences that children have gone through, and to begin a family tracing and reunification program that to date has reunified about 7,000 children. In the process of doing this, we have also closed down nine orphanages.

I would like to suggest this as a possible alternative to warehousing children in orphanages and as a model of how to work in collaboration with communities and countries to better protect the psychosocial needs of children in war situations.

Thank you.

Mr. McHugh. Thank you very much.

[The prepared statement of Dr. Boothby follows:]

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PROTECTION OF CHILDREN IN WAR AND REFUGEE SITUATIONS: TOWARDS A MORE COHERENT APPROACH

I. The "New" Face of War

In the past decade, as wars have raged in over 50 countries, the majority of victims were from poorest social classes in rural villages and small towns. But children have been the greatest victims--both as targets and as forced recruits. In World War I, civilians comprised about 5% of all casualities; by World War II, that figure rose to over 50%. In the Vietnam War, the civilian death toll rose to 80%, only to be eclisped by some of today's wars where women and children make up to 90% of all war dead.

Today's wars pose an alarming health threat to the poor, and to their children. After a decade of war in West Beirut, conditions have deteriorated so that children face violence, economic hardships, and repeated displacement as part of daily life. Families are at increased psychological risk because psychosis, depressive disorders and suicide attempts are on the rise, especially among 11 and 12 year-old youth. In Southern African countries, infant and child mortality rates have soared to the highest levels in the world as health facilities are destoyed, vaccination programs hampered, and water purification projects leveled. Five of the six nations on the U.N. list of countries most seriously affected by hunger are also embroiled in civil wars. Today's wars have produced 30 million refugees who are internally displaced or forced to live outside their country of origin. Children comprise 50 percent or more of the refugee populations.

In at least 21 countries in the past decade, children under 15 years have been used as armed combatants. Guerrilla forces often use impoverished situations to militarize villages and to recruit children into their cause. Counter-insurgents respond by destroying whole regions of the countryside, sometimes forcing survivors into relocation villages tightly controlled by the military. In other cases, rebel armies sabotage the economic base and morale of rural communities.

II. Do We Act Wisely?

Until we know how to prevent wars, the international community needs to be doing all it can to empower parents, communities and nations to protect children from the most serious physical, mental and emotional effects of war. Not only is the protection of children in armed conflicts an essential humanitarian concern in its own right, it may also be among the few viable strategies to end the terrorism and multi-generational transmission of violence that exists in some parts of the world.

When parents, communities and nations cannot be vechiles of protection on their own, the efforts of the international community may be required to protect children in war and refugee crises. Children's rights, and national and international responsibilities to ensure these rights are recognized, are articulated in the International Convention on the Rights of the Child as well as in earlier international legislation. International law offers the philosophical and political legitimacy required to work on behalf of children. But do we have the knowledge to act wisely in our efforts to protect children in war?

This was one of the principal questions we examined in our study on the subject (Unaccompanied Children in Emergencies, Oxford University Press, 1988). We found that a number of international and non-governmental organizations had sound policies and programs in the areas of primary health care and nutrition. However, there is a large policy and programmatic gap when it comes to protection of children's psychosocial well-being.

One of the study's main findings is that one-half or more of war-related family separations are not the result of parent death, but are preventable--a result of poverty, neglect, and other social, psychological and cultural causes. Yet few agencies have coherent strategies to prevent family separation or to respond to the developmental needs of children in the context of family and community. They are not equipped, in other words, to act in the best interest of the child.

Misinformed agency actions actually contribute to parent-child separations, undermine family unity, and inhibit community efforts to care for and protect its children. This occurs most often when organizations or governments rely upon orphanages or children's villages to care for children presumed to be orphans. In emergencies, orphanages and other institutional settings act as magnets, pulling boys and girls away from impoverished families. On the other hand, family reunification programs and community foster care and treatment programs are often not initiated or initiated too late to be of maximum value to children and families.

Preferential resettlement of unattached refugee children, as well as international adoption of war-affected infants and children, also undermine national efforts to care for children in their own communities. Neither resettlement or international adoption is in the best interest of the child when local placements exist or can be created. Neither will ever be an option except for the very few.

Field experience and study revealed that the care and protection of children in war and refugee situations, like many other aspects of international relief, is often provided on an improvised basis by compassionate individuals who be chance assume responsibility for meeting needs at hand. Typically, the people involved never have participated in other emergencies, nor are they aware of similar programs in other situations. Once this individual left, the same agency was often unprepared to undertake the same program in the next crisis.

III. Closing the Gap

How can we begin to close the gap between child rights as a concept and child rights as a reality? I have two basic suggestions:

First, all international and non-governmental organizations will need to become more child focused. Coherent policies based on the best interest of the child standard rather than agency preference or bias must be developed. Donors can encourage a more child centered approach to relief intervention through the establishment of funding priorities that reflect the best interest of the child standard.

Second, support will be needed for organizations that demonstrate the willingness and the ability to develop the internal capacities and expertise to actually implement programs for children in war and refugee situations. Family tracing and reunification programs, community-based foster care and treatment initiatives, and rehabilitation projects for former child soldiers are among the programs often needed and rarely implemented in emergencies. Helping to form links with child care experts and universities to assist with the development of program models, intervention strategies, and evaluation criteria will also be important.

IV. Mozambique: An Example of a More Coherent Approach

In 1988, the Office of U.S. Foreign Disaster initiated a project with Save the Children and myself to provide training and assistance in psychological assessment and treatment of displaced children in Mozambique. This program, funded through a Congressional earmark to support projects for orphans and unaccompanied children, initially focused on children who had been forced to serve as Renamo soldiers in its war against the government.

It is estimated that some 500,000 children have witnessed their families murdered during this devastating civil war. Another 200,000 are believed to be displaced from their original families. Through training efforts to date, over 500 individuals from the Ministry of Health, Mozambican Women's Organization, Gabinete Communicacao Social, police and the military have learned some of the basic ways and skills of assisting these displaced and traumatized children.

The program also works to reunify these children with immediate and extended family members. At a pilot program established at the Lhanguene Orphan Center in Maputo, families for 22 of the initial 28 children traced were located in two days. Since then, all of the Lhanguene children have been returned to their families and the orphanage closed.

With additional support from USAID and private foundations, the program has now been expanded to Gaza, Sofala, Tete, Nampula, and Cabo Delgado. Save UK and Save Norway are also implementing similar projects in Inhambane, Zambezia and Manica. To date, approximately 800 children have undergone treatment programs and more than 7000 reunited their own families. An important phase of this project provides follow-up counseling and monitoring services for the reunited children. Through this project, food, clothes and educational supplies are given not only to children returned to their own families but also to other children being cared for in substitute families. In this way, eight other orphanages have been closed down in favor of family placements.

Despite its many shortcomings, the project in Mozambique does demonstrate some of what can be done to assist children who exist in extremely difficult circumstances. It could also serve as a model for similar projects elsewhere in the world.

Mr. McHugh. Next we will hear from Mr. Roger Winter, who is the Director of the U.S. Committee on Refugees.

Mr. Winter's Opening Statement

Mr. Winter. Thank you.

I should point out that, while I wholeheartedly agree with everything my colleagues have said this morning, things could have been worse this year had it not been for the leadership that this subcommittee and its chairman took in increasing appropriations last year. What has been two years of a horrible situation for refugees generally and refugee children specifically could have been a lot worse.

It was not so many months ago, toward the end of last year, that this subcommittee increased what had been a $10 million appropriation for the emergency refugee and migration assistance fund requested by the Administration to replenish the fund at a full $50 million.

That money is rapidly going out on the firing line when it comes to assisting refugees. It simply would not have been available had this committee and its chairman not taken that leadership.

The reason we are back is because the problem is repeating itself. Phyllis and several others have already mentioned a bit of the problem. Let me just overview it in some detail. The international organizations that deal with refugees and displaced people are hurting. They are hurting badly this year. They were hurting badly last year. And that means their clientele is hurting badly.

The organizations I am talking about include the UN High Commissioner for Refugees, the International Committee for the Red Cross, the World Food Program, and the UN Relief and Works Agency for Palestine Refugees.

As others have already pointed out, some 60 percent plus of all refugees and displaced people are in fact children. The fact is that the resources for these individuals have actually been declining rapidly, plunging like a rock, over the last five or six years.

So what we are talking about is not simply trying to meet an unmet need. We are also trying to talk about forestalling a further deterioration in what is a pretty terrible circumstance.

You have already heard about massive malnutrition and increased mortality. Let me give you a couple of other examples. There are camps such as the camp called Fugnido, which is in western Ethiopia. It is the camp that Mickey Leland was killed trying to visit, along with all the staff and AID personnel last August.

There are 18,000 unaccompanied minor children in Fugnido, and over the last few months medical services and nutritional services for those children have been reduced rather dramatically because UNHCR and the World Food Program simply do not have the resources to maintain what were already inadequate levels of support.

Refugee children, as Phyllis again has already pointed out, do not have educational programs generally. In the case of Fugnido, essentially those educational programs for 18,000 unaccompanied minors have been eliminated. There almost are no educational materials any longer. There are no facilities being prepared for educational teaching.

When we talk about the Cambodian children at Site 2 on the Thai-Cambodian border, there are 58,000 children under eight just at Site 2. Less than 25 percent of them are in school. There is no school available above the primary level.

We talk about Vietnamese children in Hong Kong. Whole families as large as six people live in the space of the table behind which you are sitting. It is simply unbelievable that these kinds of conditions exist. Yet the UN High Commissioner for Refugees is in no position to remediate the problem simply because of lack of resources.

Refugees are uniquely vulnerable, as are displaced people. They have trouble helping themselves because they have been displaced from their land or from their employment, from their normal circumstances of living.

Increasingly, the UN High Commissioner for Refugees and these other organizations that I am talking about are being reduced, not to particularly helping refugee children or refugees in general, but simply to the most basic of warehousing. You may have seen the plea of the new UN High Commissioner for Refugees in the New York Times about ten days ago. This is a new High Commissioner for Refugees, already reduced to begging to try to receive the resources from governments internationally to fulfill the mandate of the organization.

FUNDING NEEDS FOR REFUGEE PROGRAMS

Secondly, Mr. Chairman, the U.S. is a factor. I am not suggesting that the U.S. is not generous. The U.S. is exceedingly generous in the way it approaches most humanitarian issues. But it is only fair to point out and to point out clearly that the U.S. percentage of support for the UN High Commissioner for Refugees, for the World Food Program, for the UN Relief and Works Agency for Palestine Refugees, and for the International Committee for the Red Cross has been dropping rapidly throughout the eighties.

Phyllis used some numbers a moment ago. Let me try to impress them on you. In 1985 there were ten million refugees in the world, and in 1985 the appropriation for migration and refugee assistance was $204 million. That equates to a per capita contribution from migration and refugee assistance to these organizations of about $20. That is in 1985.

Mr. McHugh. Excuse me. What was the total?

Mr. Winter. Total refugee population, ten million.

Mr. McHugh. Ten million.

Mr. Winter. The total appropriation, migration and refugee assistance, $204 million. That works out to a per capita figure of about $20 million.

By 1989 we had seen a 50 percent increase in refugees in the world. The refugee population in 1989 was approximately 15 million. The U.S. expenditure for migration and refugee assistance was $188 million. That is about twelve bucks per capita, and that is without any adjustment for inflation over the five-year period at all.

The problem is that our percentage for all of these organizations has been declining. We reduced our support over this same five-year period for the World Food Program from 33 percent to 23 percent. We reduced our support for the International Committee for the Red Cross from 29 percent to 15 percent of their budget.

We reduced our support for the UN Relief and Works Agency for Palestine Refugees from 40 percent to 27 percent. We reduced our support for the UN High Commissioner for Refugees from 28 percent to 21 percent.

The problem is that OMB seems to believe that there is no constituency for refugees and displaced people, and particularly children, and therefore this budget category can be squeezed. Frankly, that is why we need this committee. We need you to do again what you have done last year.

In our view, the situation is so serious that there ought to be a supplemental appropriation this year. The Administration has not requested one. It has only requested a supplemental appropriation for resettlement of refugees to the United States. What we are talking about is an infusion of funds for the International Committee of the Red Cross, the World Food Program, the other agencies I have mentioned, so that they can in fact more adequately assist refugees where they are overseas.

What we have proposed is $50 million in a supplemental to redress these cuts. The emergency fund which you helped replenish this year is currently needed to be fully utilized to deal with this year's emergencies.

Just since the 1st of January, there are 120,000 new refugees from Liberia to surrounding countries. There is the beginning massive movement of people from Ethiopia's northern provinces, Eritrea and Tigray, beginning to move into the Sudan. Since that budget was put together, there are 70,000 unanticipated Vietnamese who have gone to asylum in the first asylum countries of Southeast Asia. There are 18,000 new refugees from a very bloody and repressive situation in Burma. And so on goes the story.

What I am suggesting is that we need not only to fully utilize the emergency fund that you made available for this year, but we need to infuse funds in the system to restore the functionability of the system to meet these vulnerable people's needs.

When it comes to 1991, the President's budget makes a modest step in the right direction. But unfortunately, what it does is it only brings us back to the 1989 level of support for these institutions. 1989 was the worst year these institutions have ever had financially, and what the President's budget would do at this point is simply restore us to that level. We think that is inadequate.

What I recommend that this committee consider is approaching the migration and refugee assistance budget with two benchmarks in mind. First of all, we should really strive in 1991 to bring the per capita U.S. contribution for the programs of these four agencies to a figure of $25 per capita per year.

We should also strive to reverse the trend of declining support, so that we establish as a benchmark a minimum of 25 percent support for the budgets of the UN High Commissioner for Refugees, the World Food Program, the International Committee of the Red Cross, and the UN Relief and Works Agency.

Now, if you use that $25 per capita figure times 15 million, you simply multiply it out and it comes to $375 million for overseas assistance. The President's budget requests $215 million. That is a $160 million gap. Basically what we are requesting of you today is that you consider closing that gap seriously in 1991.

Lastly, the peace dividend that we all fondly talk about can have no better use than being used for the victims of the conflicts that have caused most of today's refugees and displaced people. What we are talking about when we talk about refugees and displaced people are the civilian victims of human conflict.

Most of those conflicts around the world today, whether it is Mozambique or Angola, whether it is Ethiopia or Afghanistan, whether it is Central America or some other part of the world, are victims of regional conflicts that in some way or other have had a relationship to the geopolitical confrontation which is now abating.

We believe that assisting the victims of those conflicts makes peacemaking very human, very personal. It brings peacemaking down to the level of the individual human being.

We ask you to take the leadership again in providing the resources to see that this is done. Thank you.

Mr. McHugh. Thank you very much.

[The prepared statement of Mr. Winter follows:]

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Informing the public since 1958

Testimony of

Roger P. Winter

Director, U.S. Committee for Refugees

on the

International Refugee Funding Crisis and its Impact on Refugee Children

Before the

U.S. House of Representatives

Committee on Appropriations

Subcommittee on Foreign Operations,
Export Financing and Related Programs

March 27, 1990

USCR is a program of the American Council for Nationalities Service

Thank you, Mr. Chairman, for the opportunity to present to the Subcommittee on Foreign Operations the views of the U.S. Committee for Refugees, a program of the American Council for Nationalities Service. I hope in this brief testimony to make three points:

> (1) Programs of the international humanitarian organizations that assist refugees and displaced people overseas, more than 60 percent of whom are children, have been crippled by massive funding shortfalls with major implications for refugee health and survival. Refugee children, being the most physically vulnerable of all refugees, are the most at risk from these cuts. While refugee numbers worldwide increased by 50 percent in the last five years, from 10 million in 1985 to 15 million in 1989, the United Nations High Commissioner for Refugees' budget increased by only 25 percent. As a result, critical services have been cut back in refugee camps throughout the world, malnutrition and mortality are on the rise, and many programs designed to assist refugee children, to preserve their opportunity to have a meaningful future, have been curtailed.
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> (2) The United States, while generous in its support of international humanitarian organizations, has allowed its share of support for UNHCR, the International Committee of the Red Cross, the World Food Program, and the United Nations Relief and Works Agency to drop steadily for much of the 1980s. For example, in 1985 the United States contributed 27 percent of the UNHCR budget, but only 22 percent in 1989. More importantly, the U.S. Migration and Refugee Assistance budget, which in 1985 provided $20 per refugee annually, now funds about half of that amount.
>
> (3) The United States should respond with at least $50 million more than is currently available this year for overseas assistance to refugees and internally displaced people. The Administration's FY 1991 budget for refugee assistance, moreover, should reverse the pattern of the last few years to meet both of two critical benchmarks. First, U.S. contributions for refugees overseas should not fall below $25 per refugee. In addition, the U.S. share of operating budgets for UNHCR and other international humanitarian organizations should not be allowed to fall below 25 percent.

Mr. Chairman, before I proceed with a more detailed discussion of these issues, I would like to acknowledge your leadership and your commitment through the years to the cause of assisting some of the world's most vulnerable populations. It was through your efforts that the emergency fund for refugee migration and assistance (ERMA) was fully replenished at a level of $50 million this year. The Administration requested only $10 million and--incredibly--seeks no additional funding for overseas refugee assistance this year. Its FY 1991 budget request restores some of what has been eroded on the overseas assistance side, but is still too low, given the explosive growth in refugee numbers worldwide. Your continued support will be critical if our country is to return to a "fair share" level of giving to overseas refugee assistance.

The Problem

For many years, in fact decades, the United States has been the largest contributor to international assistance for refugees and displaced people. On a total--though not per-capita--basis, it still is, as would be expected given our nation's size and wealth and the values of our people. However, for most of the 1980s, while the numbers of refugees and displaced people in the world have grown dramatically, the U.S. share of support for the UN High Commissioner for Refugees (UNHCR), the International Committee of the Red Cross (ICRC), the UN Relief and Works Agency (UNRWA), and the World Food Program (WFP) has diminished, in some cases dramatically. Some other governments have increased their share of contributions during this period, while others have decreased. All must continually be pressed to increase their participation. However, the sad truth is that total contributions to these agencies have not kept pace with the explosion of growth in need.

As a result of these trends, there has been dramatic impact on all of these institutions and the uprooted people worldwide who are dependent on them for protection and assistance--even survival. But the children are feeling the greatest impact:

* From 150,000 to 225,000 refugee children between the ages of 1 and 5 are suffering from acute malnutrition. "All of these children need nutritional rehabilitation," according to an internal UNHCR memorandum.

"All are in danger of death from malnutrition or subsequent infectious diseases. Unfortunately this past year it appears the number of malnourished children is rising."

° "The underlying cause of the problem," the UNHCR memo continues, "is simple but dramatic: a lack of food resources to cover the minimal components of the basic ration, namely: cereals, beans and oil....[UNHCR] has had no possibility of cushioning ration cuts by using cash resources.... In the last years, the nutritional status of refugee children has been slipping in Africa and Middle Asia...and in some countries malnutrition rates among refugee children reach 30 percent.... Famine levels range from 20-30 percent, so that any survey that shows more than 10 percent malnutrition is cause for alarm." Outbreaks of scurvy, pellagra and other nutrition-related diseases in some refugee camps are evident.

° Half the population of Fugnido refugee camp in western Ethiopia consists of unaccompanied minors, generally recognized as the most vulnerable of refugee children. Most of these 18,000 minors are boys under the age of 16. This is perhaps the largest group of unaccompanied children UNHCR has ever served. Nutrition and medical services for these children have been seriously reduced.

° The majority of refugee children have no access to primary education at all. Attempts to improve on this have been essentially suspended. Budget shortfalls have decimated educational programs for refugee children throughout Africa; schooling for Sudanese and Somali refugee children in Ethiopia is crippled by a lack of teaching materials and classrooms.

° Forty percent of the 140,000 Cambodian refugees in Site 2 camp on the Thai-Cambodian border are under the age of 8. Primary-level education is all that is available. Only 25 percent of school-aged children attend any school at all.

° Nearly 15,000 Vietnamese refugee children in Hong Kong are living in unconscionably crowded and unsanitary detention centers, and many are suffering from malnutrition and major health problems.

° Important new UNHCR guidelines for providing care and protection to unaccompanied minors in Southeast Asia, which have been years in the making, cannot be implemented due to a lack of resources.

Mr. Chairman, I have been in most of these camps. I have seen what is happening. These tragic deficiencies are not only destroying young lives right now but, for those fortunate enough to survive, will cause major damage for years to come. While many factors conspire to make the lives of refugee children more vulnerable, all of the above problems could be resolved, or substantially ameliorated, through the addition of resources.

There are many other examples worldwide, and all the other organizations I have listed also have serious shortfalls, but let me focus for a moment on one pivotal organization, the UN High Commissioner for Refugees. UNHCR is responsible to all of us for the protection and care of the world's 15 million refugees, but right now it is a crippled agency facing the worst financial crisis in its history, caused by steadily rising refugee populations and the fact that donor contributions have not risen fast enough to keep pace with the increase in numbers. These trends came to a head in 1989.

In October 1988, the Executive Committee of governments that oversee UNHCR's operations approved an initial 1989 budget for UNHCR of $429 million. It soon became clear that newly emerging needs, primarily in Ethiopia and Southeast Asia, could result in as much as a 10 percent increase in necessary expenditures. These unanticipated needs included such things as responding to the rapidly deteriorating health and nutritional situation and subsequent explosion in death rates (as high as 3,000 per month, of which most were children) that were occurring in Somali refugee camps in Ethiopia.

It also became clear in early 1989 that donor governments, including the United States, not only were not going to come up with adequate funds to meet the emerging new needs, but they were not even going to come close to covering the $429 million budget initially approved.

While protesting that critical needs of refugees would go unaddressed, UNHCR was required to reduce its 1989 expenditure target to $389 million, with $40 million of that figure unfunded and carried over into 1990 to be paid from 1990 contributions, thus heavily mortgaging UNHCR's future and that of refugees. Some $38 million in program cuts were then undertaken beginning last summer.

UNHCR's financial situation has gotten still worse. In November 1989, UNHCR projected worldwide budget needs totalling $414 million. Donor pledges for the first six months totalled only $190 million, of which $40 million went to cover deficits carried over from 1989. As a result of UNHCR's 1990 budget shortfall, now projected at $74 million, all program reserves have been eliminated. The worldwide budgets for food and water have been cut by 25 percent, sanitation by over 30 percent, shelter and infrastructure by 35 percent. One official assessment shows just what these cutbacks mean:

° Reduced buffer stocks of emergency items in some countries mean inadequate supplies of the essentials if new arrivals surge or if logistics or weather result in stalled deliveries.

° Health projects are being adversely affected; maternal and child health programs are being scaled back; some other medical services are being eliminated.

° Less water, or poorer quality water, is now all that is available to some locations.

° New school construction has been reduced significantly.

° Repair and maintenance of buildings, roads, vehicles, etc. have been dramatically reduced.

° Investment in income-generating projects has been reduced; there will clearly be fewer means of helping refugee families to become self-sufficient.

Mr. Chairman, the erosion of nutrition, sanitation, medical, and educational services in refugee camps throughout the Third World is mortally dangerous. Fundamental survival needs of refugees are not being met now; the situation is clearly deteriorating. Unless something is done now, 1990 and 1991 will be hell for too many refugees around the world, simply based on inadequate resources. Let me offer a few selected examples from Africa and Southeast Asia.

Africa

In Malawi, where one person in ten is a refugee, increases of malnutrition among Mozambican refugees have been reported from 5 to 15 percent in a year, primarily because of UNHCR's inability to establish a buffer stock or to pay for the grinding of maize.

Malnutrition in refugee camps in the Sudan is up to 20 percent, and as high as 30 percent in Somalia. According to the UNHCR memorandum cited previously, "poor nutritional status has made refugees more vulnerable to outbreaks of communicable diseases such as meningitis, cholera and hepatitis that have been seen in 1989 in Somalia, Malawi, Sudan, and Ethiopia."

Southeast Asia

Of the 540,000 refugees in Southeast Asia, the largest number are Cambodians, of whom 300,000 are camped precariously just inside the Thai border. The largest refugee camp in Southeast Asia is Site 2, where 140,000 Cambodians wait for a chance to go home safely. With a birthrate of more than 7 percent, nearly 40 percent of the population is under the age of eight, and 27 percent under five.

Home for these children is in a war zone. They are vulnerable and frequent witnesses to shellings, shootings, beatings, and the grinding pressure of immobility and monotony. Services are minimal. Chronic malnutrition (stunting) is a significant problem. Primary school is the only level available, and that for only 25 percent of the children. Water has been at half-rations since January.

Thailand has signalled that it might move the border population to safer, neutral camps farther from the fighting. While that is an encouraging step, the real answer is to negotiate peace in Cambodia and help these people get home safely. Both options will cost serious money.

Regionally, as part of the Comprehensive Plan of Action (CPA) endorsed last summer in Geneva, the UNHCR is to implement new guidelines to protect and care for the substantial number of Vietnamese unaccompanied minors. Principal among the CPA initiatives is to establish committees with child welfare expertise in each of the asylum countries--Thailand, Malaysia, Hong Kong, Indonesia, and the Philippines--to decide on an expedited case-by-case basis what is the best durable solution for each minor. But after nine months, only two countries have established committees--UNHCR resources, again, are a large part of the problem--and these children just wait.

Nearly 15,000 Vietnamese children in Hong Kong are living in crowded and unsanitary detention centers and many are suffering from malnutrition and major health problems, according to a recent report from the Women's Commission for Refugee Women and Children. "Major problems exist regarding assistance to and protection of these children," the report says. "The health status of the children is particularly troubling. A UNHCR survey has identified widespread malnutrition. Most children we observed had scabies and are subject to other ailments including childhood diseases such as measles."

Access to the limited health care available has also been a problem. The camps in Hong Kong are administered by the Correctional Services Department. In other words, Vietnamese asylum seekers and their children are in jail. One woman described the terms of her sentence this way:

> When our children wake up at night and need medical help, we ask the orderly if he will take us to the health station. He tells us no. We ask for vitamins, they tell us no. My friend had to give birth in the camp because she was too early. She got no treatment for the child and her child died. All we hear is No! No! No! We feel no protection coming from the orderlies or from the police.

The United States is a Key Factor

I am not suggesting that the United States is uniquely the problem here. The U.S. approach to these issues is clearly among the most generous in the world. It is also clear, however, that U.S. funding practices during the last few years relate directly to the funding crisis at UNHCR and major shortfalls at the other agencies. The overall U.S. budget is exceedingly tight; new needs have arisen and commitments have been made; the refugees we are discussing suffer--without a strong constituency--out of sight and out of mind.

Most U.S. support for refugees is included in the State Department's Migration and Refugee Assistance (MRA) account, although resources from AID, the Emergency Refugee and Migration Assistance (ERMA) fund, and other accounts can be brought to bear to some degree and under certain circumstances.

In 1985, the worldwide refugee population was just over 10 million people. By 1989, the number had increased by 50 percent to 15.2 million (see Table A). In this same period, the line-item in the MRA budget for refugee assistance shrank from $204.4 million to $168.7 million. On a per-capita basis, unadjusted for inflation, the State Department's MRA refugee assistance budget provided $20 per refugee in 1985 and only about $12 per refugee in 1989.

It is hardly surprising then that U.S. contributions to UNHCR, UNRWA, ICRC, and the World Food Program, as a percentage of total budgets for these organizations, has declined dramatically (see Table B).

U.S. support for UNHCR was as high as 30 percent of total expenditures in 1982, even higher before the 80s. From 1985 to 1989, the U.S. share dropped from 27 percent to approximately 22 percent. Thus, the United States was supporting less of UNHCR even as UNHCR resources, on a per-capita basis, were declining. While UNHCR's caseload was increasing by 50 percent, the U.S. contribution to UNHCR grew by only 2.3 percent.

U.S. support for UNRWA dropped from 40 to 27 percent of total expenditures from 1985-1989. For ICRC, U.S. support dropped from 30 to 15 percent of total expenditures from 1985 to 1988, almost writing off this critical agency that often is alone in serving internally displaced people, especially in Africa. In the early 1980s, U.S. support for ICRC was as high as 40 percent of total expenditures. The World Food Program has seen U.S. support for its programs decrease from 28 percent to less than 23 percent from 1985 to 1989.

Mr. Chairman, despite the real commitment to refugee assistance within some sectors of the Administration, we believe that for a number of years, the Office of Management and Budget has been systematically and cynically targeting the overseas refugee assistance account for cutbacks on the assumption that it has no strong constituency to work in its defense. You have proved them wrong in the past. It is time to do so again.

Refugee Assistance Needs in 1990

The failure of the international community to fund UNHCR budget needs in full--as well as those of other international humanitarian organizations--is sapping the institution's strength and resources. It reached crisis proportions last year, continuing into this year. At the field level, staff don't even ask for resources to meet real needs because they know the funds are not available. As this process plays out, the most vulnerable refugees, often at the edges of the response system, away from TV cameras, begin to suffer immensely or to die. Then, when a substantial new problem arises--an increase in numbers or a drop in funding--there is no reserve capability to employ in response.

The Administration has told you that if an additional $70 million is provided this fiscal year to admit another 27,000 refugees for resettlement in the United States, then the $50 million in ERMA funds will be sufficient to meet refugee assistance needs. We disagree. ERMA funds should be obligated in full to meet the "urgent and unforeseen" needs that have arisen this year, but--beyond all currently available resources--an additional $50 million will be needed to address the budget shortfalls of the UNHCR, UNRWA, WFP, and ICRC.

Refugee emergencies are happening constantly. It's the name of the game. Among the many urgent needs and opportunities that require ERMA funding in 1990 are the following:

° Conflict in Liberia has resulted in more than 120,000 refugees fleeing to the Ivory Coast and Guinea since the beginning of 1990.

° The first of what could be a very torrent of people have left northern Ethiopia and entered Sudan in flight from the conflict and impending famine.

° In southern Sudan, the town of Juba with 300,000 residents is under siege. More refugees have fled the fierce fighting there and entered Uganda. The Sudanese refugee camp at Asosa in Ethiopia has been destroyed.

° An unanticipated influx of 70,000 Vietnamese refugees in Southeast Asia has overstrained camp services and accelerated the demand for implementation of the costly Comprehensive Plan of Action ratified by 76 nations, including the United States last June in Geneva.

° More than 18,000 Burmese refugees have spilled across the border into Thailand since the beginning of the year, fleeing from Burmese army attacks on ethnic minority groups and pro-democracy activists. They are in desperate need of international aid and protection.

° Prospects exist in 1990 for the repatriation of refugees from Nicaragua, South Africa, Ethiopia, El Salvador, and possibly Mozambique and Cambodia. Repatriation is the best permanent solution for refugees. Should these opportunities arise, money must be available to help them get home. UNHCR special appeals for repatriation funds in 1989 were underfunded by more than $22 million.

There are, moreover, six months left in the fiscal year, and new needs and opportunities undoubtedly will present themselves. If ERMA funds are obligated for urgent and unforeseen needs, as they are supposed to, then there will be no resources available to restore basic level services in refugee camps throughout the Third World. The United States should not have to choose whether to do one or the other. We must do both. Other governments are now starting to recognize their own responsibilities in this regard.

The United States should be supporting overseas refugee assistance at a level which both remedies the systemic failure that has set in, and provides the needed resources to respond to unanticipated emergencies, including substantial but costly repatriation we hope will occur with the geopolitical thaw.

To restore FY 90 U.S. contributions to UNHCR, UNRWA, and ICRC to FY 89 levels, and in so doing at least partially restore the across-the-board cuts in essential services, will require an additional $50 million.

The only way to get this additional money is to secure a FY 1990 supplemental appropriation for both resettlement admissions and overseas assistance, $70 million and $50 million respectively. In addition, ERMA funds must be fully obligated to meet urgent needs in 1990. In other words, the United States must spend at least $100 million on refugee assistance this year, over and above the $168 million that currently is available within the MRA account.

The 1991 Budget

In addition to meeting emergent 1990 needs, the United States should reverse its pattern of diminishing support for these international humanitarian institutions. The President's 1991 budget for overseas refugee assistance is a very modest step in the right direction. I say modest because his request essentially only returns us to the 1989 level of Migration and Refugee Assistance support, without even accounting for inflation or the increased refugee population worldwide. But 1989 was a disastrous year in terms of refugee funding. Frankly we need to do better.

I propose that the U.S. establish a goal that would permit us to lead the world back to adequate support for the world's refugees. We can do this by setting, and meeting, both of two benchmarks in refugee assistance. First, we should ensure that U.S. MRA contributions for refugees overseas do not fall below $25 per refugee. Second, the U.S. share of UNHCR expenditures and those of other international humanitarian agencies should not fall below 25 percent. These figures would of course need to be adjusted periodically for inflation.

In 1985, the State Department's Migration and Refugee Assistance budget provided about $200 million to serve 10 million refugees worldwide, or about

$20 per refugee. To maintain that level today, adjusting for inflation, would require about $25 per refugee. In fact, the refugee assistance budget now provides only about $12 per capita.

Twenty-five dollars times 15 million refugees comes to $375 million, whereas overseas assistance is only budgeted in the President's 1991 budget at $215 million. Effectively, the gap for 1991 is $160 million, assuming the worldwide refugee population remained constant. I, therefore, encourage you to consider an FY 1991 MRA appropriation of $610 million for both admissions and overseas assistance, with full replenishment of ERMA. We should get to the place where ERMA is again an emergency fund and not used for ongoing services.

Mr. Chairman, in closing, I would like to focus on the abatement of geopolitical conflict in our world and its implications for refugees. Most of the refugees we see throughout the world today have fled from civil wars connected to this ideological struggle between the U.S. and the USSR that has gripped the world these last 40 years. Each day brings new evidence that that struggle is abating. But the victims of those wars should not be neglected.

One candidate for a peace dividend must be an augmented refugee assistance budget. Providing additional funding for large-scale repatriation, and drawing it from scaled-down defense spending, would signal United States resolve to help those who have been hurt in regional conflicts.

It seems to me that the objective of the U.S. in regard to the 1991 budget should be (1) to reverse the downward trend in assistance funding for refugees in first asylum and thus to reverse American decline in leadership in this crucial arena of foreign aid; and (2) to assure that funds are available to permit large-scale voluntary refugee repatriations should the opportunities arise.

Mr. Chairman, what better way to signal to the Soviets and to the world our intentions to proceed with regional conflict resolution, than to provide for those who have suffered for the past decade in first asylum? I ask you and your colleagues in the House and Senate to introduce this line of reasoning to the forthcoming debates on the 1991 budget.

Thank you.

TABLE A

Year	Number of Refugees Worldwide*	U.S. Migration and Refugee Assistance Budgets (in millions)		
		Admissions	Overseas Assistance	Total**
1985	10.1 million	$103.2 actual	204.4	350.3
1986	11.7 million	105.3 actual	189.7	324.4
1987	13.3 million	108.7 actual	194.7	346.9
1988	14.4 million	119.5 actual	176.2	338.5
1989	15.2 million	225.0 actual	188.3	462.0
1990	N/A	156.0 estimated	168.7	368.4

Percent of Change, 1985-1989

In Number of Refugees	In Admissions	In Overseas Assistance	In Total Expenditure
50% increase	118% increase	7% decrease	32% increase

* Source: U.S. Committee for Refugees

** Total also includes budget line-items for refugees to Israel, other international organizations, and administration.

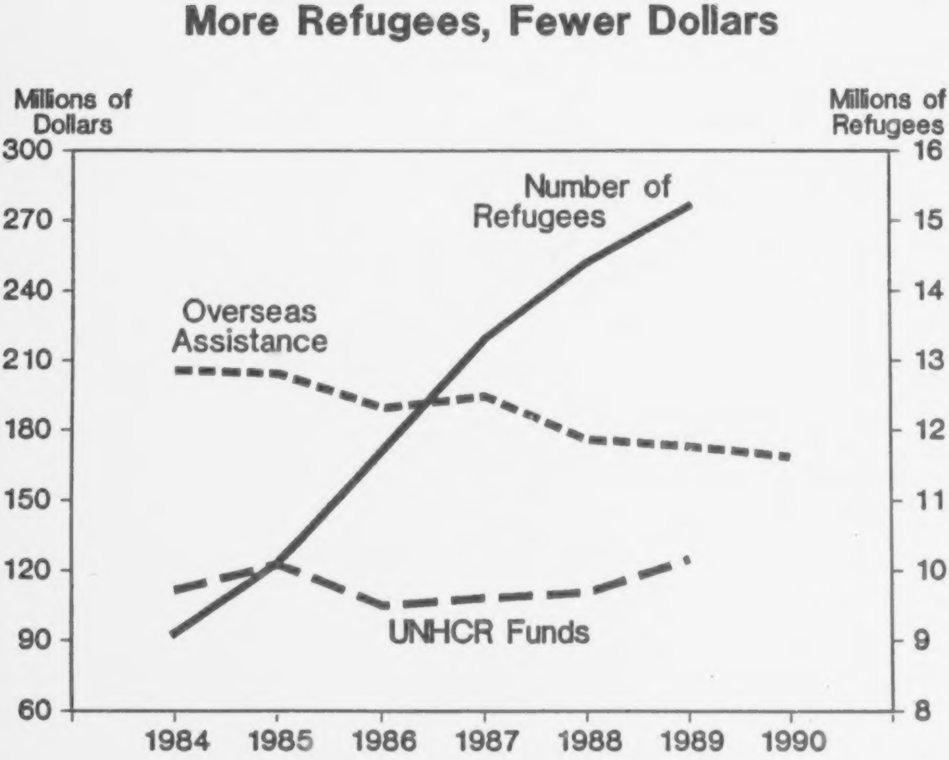
TABLE B

Percent of U.S. Support for International Humanitarian Agency Expenditures

	UNHCR	UNRWA	WFP(all purposes)*	ICRC
1984	25.15%	35.02%	33 (1983/1984)	29%
1985	26.77	40.02	28 (1985/1986)	30
1986	23.86	35.92	28 (1985/1986)	26
1987	23.56	33.45	22 (1987/1988)	21
1988	21.78	29.08	22 (1987/1988)	15
1989 est	21.89	26.96	23 or less (1989/1990)	NA

*World Food Program operates on a two-year budget.

TABLE C



Overseas assistance funds from U.S. Migration & Refugee Account.
Source: House Select Committee on Hunger

THE U.S. COMMITTEE FOR REFUGEES

REPRINT

THE NEW YORK TIMES INTERNATIONAL SUNDAY, MARCH 18, 1990

U.N. Aide Fears Help for Refugees Will Fall Short

By PAUL LEWIS
Special to The New York Times

GENEVA — The number of refugees in the world has doubled in the last decade, but the international organization charged with caring for them is facing a growing financial crisis.

Thorvald Stoltenberg, the former Norwegian Foreign Minister who took over as the United Nations High Commissioner for Refugees three months ago, estimates that he will need more than $700 million this year to look after the world's 15 million refugees. But he anticipates no more than $550 million from countries with financial constraints of their own.

"I can't fulfill my mandate," he said in a recent interview at his headquarters here. "Levels of care are falling. I have only half the resources per refugee today that we had in 1980."

Others share Mr. Stoltenberg's concern. Roger P. Winter, Director of the United States Committee for Refugees, told the House Committee on Hunger last month that the number of refugees rose 50 percent in the last five years but that the United Nations refugee agency's budget increased only 25 percent, while the United States' share fell to 22 percent from 27 percent. "As a result critical services have been cut back in refugee camps throughout the world," Mr. Winter told the House.

While Mr. Stoltenberg's predecessor, Jean-Pierre Hocké, had a reputation as an abrasive manager who got personally involved in day-to-day refugee operations, Mr. Stoltenberg says he plans a different approach.

Day-to-day management will be left to Douglas Stafford, the new American Deputy High Commissioner. Mr. Stoltenberg says this arrangement will leave him free to seek money and what he calls "political solutions."

The number of refugees in the world climbed from about 7 million in 1980 to about 10 million by 1985 before reaching 15 million today, largely as a result of continuing civil strife in Africa, Central America, Afghanistan and Cambodia and the exodus of boat people from Vietnam. An insurrection in Liberia earlier this year sent 120,000 more refugees into the Ivory Coast and onto the High Commissioner's books.

Reserve Fund Exhausted

As the refugee crisis has grown, the High Commissioner's budget has risen, but never by enough to meet the new claims being made on it. The agency gradually drew on a reserve of about $85 million.

By 1988 this fund was exhausted. The High Commissioner's budget fell $7 million short of requirements in 1988; the deficit rose to $38 million the next year, and it is expected to reach $150 million to $200 million in 1990, said John Horekens, the head of fund-raising services.

As a result, the level of help and protection offered refugees is being steadily cut back. An internal memo of the refugee agency dated Nov. 30, 1989, notes that "150,000 to 225,000 refugee children are suffering from acute malnutrition. All of these children need nutritional rehabilitation. All are in danger of death."

The agency's Head of Program Management Services, Gerald Walzer, told the House Hunger Committee last month that he was forced to provide less education for refugee children, reduce the quality of water in some camps and restrict "basic items such as blankets, tents, shelter material, cooking utensils, heating and cooking fuel."

The new High Commissioner says he hopes to encourage new donors to contribute, including the Gulf Arab states, which give almost nothing, although close to half the world's refugees are Muslims. He also says he hopes the Soviet Union, the new democracies of Eastern Europe and the industrializing countries of southeast Asia will become more generous.

But with money hard to find, Mr. Stoltenberg also plans to put new emphasis on "political solutions." This means a drive to negotiate the voluntary return of Vietnamese boat people and other refugees, as well as intervening early in political crises to prevent large migrations and further strains on the agency's budget.

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Mr. McHugh. Father Harvey, you have been patient. There is always some disadvantage in being at the end of the line, but we appreciate your being here. We would be delighted to hear from you now.

Reverend Harvey's Opening Statement

Reverend Harvey. Thank you, Mr. Chairman.

This is one time that I am grateful to be last, because I am speaking about a very specific issue, but it would be important only because of the kind of global issues that were addressed by my colleagues, and I can only say on behalf of Catholic Charities that I support all the recommendations that were made.

I am the Executive Director of Catholic Charities USA, which is a federation of 633 social service agencies affiliated with the Catholic community in the United States. That may raise a question as to why the interest in today's panel, and I might mention last year we benefited through providing some kind of service about nine million people in the United States.

About half of those were for food and shelter, so you see we feel a solidarity with those who are in extreme conditions in the third world and other places. But I think a large part of our poverty clientele in this country does come from the new immigrant, from the refugee, and from those who have been marginated by world conditions, and that too gives me an interest.

I also represent Catholic Relief Services and Caritas Internationalis, which is a 120-nation confederation of Catholic social service, relief, and development organizations. Among those statistics I mentioned to you, Catholic Charities gave service to 43,141 women in the United States who were dealing with some problem concerned with pregnancy. We were involved in the completion of about 4,285 adoptions, of which 755 were for special needs children and 772 were inter-country adoptions.

INTER-COUNTRY ADOPTION

Dr. Boothby mentioned that often an inter-country adoption is as much a problem and a cause of family breakup as it is a reward, and it is to that subject I want to speak. If we look at the statistics of just one organization like Catholic Charities, where you already glean out the number of adoptions and you see in one social service system 80 to 90 percent of women that are having babies in difficult situations are choosing to keep them, you have a tremendous "consumer demand", which is creating a shift in our fundamental philosophy, not ours but nationally, in moving from the focus of the child at risk or the young woman who is in a difficult circumstance to the consumer need of a sterile couple.

It is that need that is putting pressure on third world babies that are living at risk, and it is to that that I would like to speak. I limit my remarks primarily to Latin America, but even in doing so I acknowledge that that too is a problem because it shows the racial selectivity of where people turn to find babies, and right now that is primarily parts of Asia and Latin America, rather than Africa, which is living in more extreme circumstances.

Every year thousands of refugees from the third world, especially from Latin America, are placed for adoption outside their countries of origin illegally or inappropriately. It is estimated that at least 1,000 of these children are placed in the United States.

Now, that is an extreme statistic on the difficult cases. A pediatrician that works for the Organization of American States told me that he estimates that private adoptions in general have gone from about 500 in 1980 to about 10,000 last year.

So we are seeing a growth, not in the mammoth proportions of some of the disease factors and other things that are placing children at risk, but we are seeing an area that is non-regulated and is subject to abuse, and I think your committee in dealing with the global proportions of children in the third world may want to look carefully at that reality.

I will not repeat a lot of the statistics, but let me just suggest in Latin America about 40 percent of the population are presently 14 years or younger. Experts on the subject estimate—and it is an estimate because it is hard to count—that about 35 million on the continent, children, are living in terrible circumstances, and maybe as high as five million are living independently, either in the streets or in very large orphanages.

The problems are exacerbated by the dislocation of people from the more rural communities to large urban complexes, where they live in the adverse conditions already described: the pauperization of women, the civil wars that exist in some places, the international wars that exist in others, all of which tend to create a tremendous pressure on the children of Latin America.

CATHOLIC CHARITIES AND LATIN AMERICAN ADOPTIONS

I would like to speak to a collaborative effort that Catholic Charities in the United States has been involved in since 1984. We have reached out to our counterpart organizations in a variety of nations in Latin America to try to set up a dialogue that might lend itself to some problem resolution.

Representatives of United States organizations are gravely concerned about the large number of Latin children who are being brought to the United States for adoption without adequate professional social work involvement or evaluation. Many of these children are being placed in homes of families which have been rejected from consideration by adoption agencies within the United States. Some of the adoptive families themselves have been victimized by unscrupulous entrepreneurs, whose primary motive in arranging the adoption is for profit rather than the best interests of the children. When you have this kind of consumer demand, exploitation is very easy.

The United States agencies are deeply interested as well in the situation of the much larger number of Latin American children who will remain in their own countries of origin regardless of how many participate in inter-country adoptions. Certainly a program of both aid and development is warranted to improve the conditions under which needy children and their families are forced to live and to extend some hope to them for a more positive and productive future. For that reason, I support all the statistics and the requests that have already been made of you.

Catholic Charities USA has formed an international child care and placement program with the Migration and Refugee Services of the American Bishops Conference and a group of agencies in Latin America and in Geneva, in Rome, in Europe, where we have international representation, to coordinate child welfare efforts under the auspices of United States-based Catholic social welfare organizations.

The counterpart Catholic organizations of Latin America are well aware of the intolerable and inhuman conditions to which the homeless, abandoned, or orphaned refugee of that continent are subjected, and also of the illicit trafficking of refugees which is rampant in most of their respective countries. However, they also represent a culture where adoption itself is a foreign concept.

They prefer to have the extended family take responsibility and, while that is great in principle, when you get in the kind of dislocations we are talking about it oftentimes is more an ideal than the reality.

These same organizations in Latin America have raised serious questions regarding international adoption programs designed to benefit homeless children of Latin America. They hesitate to see their continent's most precious resource, the children, being transported to foreign lands and cultures, especially in the industrialized northern countries.

They fear the potential for additional graft and corruption in such programs. They question why such minuscule resources are channeled to the children who remain in their countries of origin and, on the other hand, they readily acknowledge that the numbers of Latin American children without families continue to grow explosively, and that only a truly concerted effort on a worldwide basis can even begin to search for adequate solutions to the problem.

In view of the critical situation outlined above, we perceive the need for an intensive collaboration among child welfare and adoption experts in various United States and Latin American organizations, both Catholic and otherwise, devoted to promote justice and full human development to all peoples. In Catholic Charities our mission demands that we strive not only to preserve life, but to ensure an adequate quality of life among all children.

CONSIDERATIONS IN INTER-COUNTRY ADOPTIONS

For those children being placed in international adoption, we must encourage their placement in homes which receive professional guidance and support, which preserves the Latin American cultural identity of the children. For the majority of needy children who remain in their countries of origin, we must also discover the means to promote the full and free realization of their God-given potential.

As a result, the international organization we formed which is called "International Child Care & Placement" has the following goals:

First, to establish and help fund low-cost child welfare programs in Latin America that would help biological families keep their children and all that goes with that;

Secondly, to facilitate and subsidize domestic adoption in those countries by the children's relatives or by local families previously screened by local certified adoption agencies. In other words, the second objective is to keep the child in his or her own country.

And thirdly, and only after those two objectives have been exhausted, to make available the alternative of agency to agency inter-country adoptions for those children legally free for adoption and who cannot be placed in their own countries.

There are a few general considerations in this area that I would also like to address. Why should we place much concern about inter-country adoptions when we can benefit a greater number of children by concentrating on child welfare programs abroad? I have already mentioned we see it only as the last alternative because we agree, as Dr. Boothby said, that it is really a disruption. But as long as it is happening, it is going to need some regulation and control to keep exploitation to a minimum.

We strongly advocate agency to agency placement when inter-country adoption is the only alternative left for a child without a family, and we also opt for private adoptions, if they are not agency to agency, that they are subject to some kind of regulation of international and national law.

I would also like to suggest that United States legislation should be adopted to facilitate adoption procedures conducted in foreign countries as long as there is proof that the judicial proceedings required by the foreign country have been met. The best evidence of that would be an authenticated certificate from the country with foreign jurisdiction. I will give an example of why that is a problem.

In many cultures, biological parents have no paternal rights unless paternity is legitimated. The mother in that case can legally place her child for adoption in that country. American citizens, however, cannot bring the child into the United States, even if legally adopted abroad, because under current U.S. law that child is no longer an orphan, by a technicality of the local country's law.

The result is that persons from European and other countries can legally adopt these children, while American citizens have no opportunity to do so.

We also feel that children adopted abroad should be considered like any American adoptive child and be given the benefit of tax credits. And foreign children with emotional or physical handicaps, such as spina bifida, should qualify for adoption into the United States without immigration restrictions.

U.S. AID FOR CHILDREN

It is important to notice that, perhaps with some exceptions, U.S. foreign aid does not focus on children, and it is for that reason that we in Catholic Charities do commend you, the members of this subcommittee and its chairman. We strongly suggest that you earmark more foreign aid to the third world and Eastern European countries for child welfare and child protection services.

I would suggest five things in the framework of that aid to relieve the conditions that create the problems:

First, to have efforts always focus on that which will strengthen family unity and not lead to further separation and disruption, as has already been mentioned;

Secondly, training local people to provide social and professional services to handle their own needs as much as possible;

Thirdly, creating culturally appropriate nutrition programs tied up with the local economy;

Fourthly, developing indigenous adoption and foster care programs to move away from the idea of caring for children in large institutions, which is growing in popularity, especially in Latin America, to place as many children with local families as possible;

And fifthly, creating a crisis emergency fund that could be used to provide help for children on short notice.

Thank you very much for this opportunity.

[The prepared statement of Reverend Harvey follows:]

TESTIMONY MARCH 27

TESTIMONY OF REVEREND THOMAS J. HARVEY, EXECUTIVE DIRECTOR CATHOLIC CHARITIES USA TO THE APPROPRIATIONS SUBCOMMITTEE ON THE SUBJECT OF HELPING REFUGEES AND CHILDREN.

I AM REVEREND THOMAS J. HARVEY, EXECUTIVE DIRECTOR OF CATHOLIC CHARITIES USA. CATHOLIC CHARITIES IS A FEDERATION OF 633 SOCIAL SERVICE AGENCIES AFFILIATED WITH THE CATHOLIC COMMUNITY IN THE UNITED STATES.

IN 1988 THESE AGENCIES PROVIDED VARIOUS SERVICES TO 43,141 WOMEN DURING PREGNANCY. THEY WERE INVOLVED IN THE COMPLETION OF 4,285 ADOPTIONS OF WHICH 755 WERE FOR SPECIAL NEED CHILDREN AND 772 WERE CHILDREN FROM OTHER NATIONS.

ONE ASPECT OF THE PLIGHT OF CHILDREN IN DEVELOPING COUNTRIES

Every year thousands of children from Third World countries, especially from Latin America, are placed for adoption outside of their countries of origin illegally or inappropriately. It is estimated that at least one thousand of these children are placed in the U.S.

A large number of these "private" adoptions are made without any professional care for the needs of the children, without proper supervision and also without any post adoption services for either the children for the adoptive parents.

The organizers of this market can make a 5 to 10 thousand dollar profit per child and a lot more in many cases.

BACKGROUND OF THE SITUATION IN LATIN AMERICA

About 40% of the expansive population of Latin America is now under 14 years of age. Even with an expected decrease in the fertility rate, it is projected that by the year 2000, 30% of the Latin American population would be younger than 15.

This demographic process of expansion is intimately linked to the phenomenon of critical poverty. Thus, within the very large number of children being born, there are millions who remain marginated from the process of economical and social development of their countries.

Recent estimates indicate that there are currently more than 35 million children under six years of age suffering from conditions of poverty in this region, with a projected figure of 51 million by the year 2000.

Poverty in Latin America is increasingly becoming an urban phenomenon due to a rapid urban population growth combined with rural-urban migration. Currently two thirds of the region's population lives in urban areas. It is within this context of poverty that we find the marginal urban family struggling to survive amidst such conditions as unstable jobs or a total lack of them; pre-marital unions affected by alcoholism and by a high reproductive index; lack of education; crowded living conditions; promiscuity; juvenile prostitution and other social problems. As a result, numerous pregnancies culminate in the birth of children whose mothers are ill-prepared for motherhood, and for whom the abandonment of the child appears as the only possible alternative. Many other pregnancies often end in abortion for the same reasons.

In spite of the magnitude of the problem, it is very difficult to obtain statistics about abandoned children, street children or children placed in institutions in Latin America, because most countries do not keep reliable records. However, most experts agree that the figure of 35 million children at risk, due to their critical situation of poverty, is accurate.

(Excerpted from Manual De Procedimientos Para La formacion De La Familia Adoptiva, Francisco Pilotti, Inter-American Children's Insitute, Montevideo, Uruguay, April, 1988.)

THE EFFORTS OF THE CATHOLIC ORGANIZATIONS TO ADDRESS THIS SITUATION IN LATIN AMERICA

Since 1984, periodic contacts have been made between Catholic Charities organizations in the United States and the various Caritas and other Catholic Church related social welfare organizations of Latin America with regard to the desperate plight of homeless and abandoned children in the continent.

Representatives of the United States organizations are gravely concerned about the large numbers of Latin American children who are being brought to the Unites States for adoption without adequate professional social work involvement and evaluation. Many of these children are being placed in homes of families which have been rejected from consideration by adoption agencies within the United States. Some of the adoptive families themselves have been victimized by unscrupulous entrepreneurs whose primary motive in arranging adoptions is that of profit rather than that of the best interests of the children. The United States agencies are deeply interested, as well, in the situation of the much larger number of Latin American children who will remain in their countries of origin. Most certainly, a program of both aid and development is warranted to improve the conditions under which such needy children and their families are forced to live and to extend some hope to them for a more positive and productive future. For the purpose of addressing these serious issues, the United states Bishops' Conference (Migration and Refugee Services Office), in conjunction with Catholic Charities USA, established the INTERNATIONAL CHILD CARE AND PLACEMENT PROGRAM to coordinate child welfare efforts under the auspices of the United States-based Catholic social welfare organizations.

The counterpart Catholic organizations of Latin America are well aware of the intolerable and inhuman conditions to which the homeless, abandoned, or orphaned children of that continent are subjected and also of the illicit trafficking of children which is rampant in most of their respective countries.

These same organizations have raised serious questions regarding international adoption programs designed to benefit the homeless children of Latin America. They hesitate to see their continent's most precious resource - its children - being transported to foreign lands and cultures. They fear the potential for additional graft and corruption in such programs. They question why such minuscule resources are channeled to the children who remain in their countries of origin. On the other hand, they readily acknowledge that the numbers of Latin american children without families continue to grow in exponential proportions and that only a truly concerted effort, on a worldwide basis, can even begin to search for adequate solutions to this problem.

In view of the critical situation outlined above, we perceive the need for an intensive collaboration among child welfare and adoption experts of the various United States and Latin American Catholic organizations devoted to promote justice and full human development among all peoples. Our mission demands that we strive not only to preserve life but also to insure an adequate quality of life among all children. For those children being placed in international adoption, we must encourage their placement in homes which receive professional guidance and support and which preserves the Latin American cultural identity of the children. For the majority of needy children who will remain in their countries of origin, we must discover the means to promote the full and free realization of their God-given potential and dignity.

The ICCP has the following goals:

1. To establish and help fund low cost child welfare programs that would help biological families keep their children, thereby supporting and promoting the rich tradition of family care and extended families that exists in many developing world cultures. Family oriented programs staffed with local social workers or volunteers (and with some help from the U.S.) could help improve the quality of these families' lives through education about such basic issues as nutrition and health care. Programs to teach parents basic skills suitable for the local economies could help break the cycle of poverty.

2. To facilitate and subsidize domestic adoptions, by the children's relatives or by local families previously screened by locally certified adoption agencies.

3. To make available the alternative of agency-to-agency intercountry adoptions under Catholic auspices for those children legally free for adoption and who cannot be placed in their own countries.

The lack of adequate funding has been a frustrating factor. We are currently planning a collaborative fundraising effort that, we hope, will provide a modest source of money to finance some child welfare programs in the Third World.

GENERAL CONSIDERATIONS

Why so much concern about intercountry adoptions when we can benefit a greater number of children by concentrating on child welfare programs abroad?

We feel that the percentage of children being adopted abroad should not be forgotten, not matter how small the number in proportion to those in need of attention.

The church does not promote intercountry adoptions, but given the realities created by the unequal social conditions of our world and the adoption market created by those circumstances, we strongly feel that these children should be offered a humane, professional, legal, and ethnically sensitive alternative, in opposition to the non-regulated private adoptions.

Private adoptions are often profit-making oriented and lack the professional support system that only professional adoption agencies can offer to both the children and the adoptive parents. Also, by operating without proper supervision, their promoters often serve adoptive "parents" that have been rejected, in many cases, by properly trained adoption professionals, thus increasing the potential for family breakdowns as a result of poor motivations or lack of preparation of the adoptive parents.

When these cases are publicized by the media it only helps to reinforce the image of the "ugly baby buyer American".

- We strongly advocate for agency-to-agency placement when intercountry adoption is the only alternative left for a child without a family.

- Private adoptions should be regulated by law to conform to the same professional standards of certified adoption agencies or banned all together.

OTHER POSSIBLE REQUESTS TO FACILITATE ADOPTIONS FROM ABROAD

U.S. Legislation should be adopted to allow adaption procedures conducted in foreign countries as long as there is proof that the judicial proceeding required by the foreign country have been met. the best evidence would be an authenticated certificate from the court with foreign jurisdiction.
For example, under many cultures biological parents have no paternal rights unless paternity is legitimated. The mother, in that case, can legally place her child for adoption. American citizens, however, can not bring that child into the U.S. (even if legally adopted abroad) because under current U.S. law, that child is not an "orphan".

The result is that persons from other countries can legally adopt these children while American citizens have no opportunity to do so.

- Children adopted abroad should be considered like any American adopted child for tax credit purposes.

- Foreign children with emotional and/or physical handicaps (e.g. spina bifida) should qualify for adoption into the U.S. without immigration restrictions.

FINAL REMARKS

It is important to notice that, perhaps with only some exceptions, U.S. foreign aid does not focus on children.

We strongly suggest to earmark some of the U.S. foreign aid to Third World and Eastern European countries for child welfare and child protection programs.

Some of this proposed aid could be used for:

Enhancing efforts which strength the family unity:

- training local people to provide social and professional services to children.
- creating culturally appropriated nutrition programs tied up to the local economy.
- developing indigenous adoption and foster care programs to place as many children with local families as possible.
- creating an emergency fund that could be used to provide help for children in a short notice for crises.

Mr. McHugh. Thank you, Father.

Thanks to all of our panelists for some very eloquent statements. I think it is safe to say that this committee is very sympathetic and is anxious to be very supportive within the context of our own budget.

We are facing a bit of a time crunch here because we have our next panel of witnesses at 11:00. It is now ten to 11:00, and I want to give Mr. Lehman five minutes for his questions.

Let me ask first, however, if any of you have any additional brief comments based on testimony which others have given, any other reaction, points you would like to add or fill in?

[No response.]

U.S. AID FOR CHILDREN AND REFUGEE PROGRAMS

Mr. McHugh. If not, let me say first of all by way of explanation—and this is something I suspect the chairman might point out if he were here—within the framework of our total budget, foreign aid, as you know, is very limited. I think we spend about 1.5 percent of our total budget on foreign assistance.

Within that limited budget there are enormous competing interests, as you can expect. One of the problems we face this year is that the demands on the foreign aid budget are increasing with Eastern Europe, Nicaragua, and Panama. Mrs. Aquino refused to see our Secretary of Defense because she and her government were very disappointed in the amount of money they got last year, and so that is symptomatic, I am afraid, of the kind of strains we are under.

As I look at this budget, it is very difficult to see how there will be much additional money for foreign assistance in the aggregate. I think that that is not likely to change until we have a realistic and practical resolution to our macro issue and the larger budget questions, because even though some of these programs, which are very deserving, have sustained some reductions, we have domestic programs in some cases that have been eliminated.

Back home we have county governments in my district that have increased their property taxes 42 percent in one year, in part because they are not getting the kind of Federal assistance they once got. Revenue sharing money, for example, was totally eliminated in the prior year's budget.

And so, domestic programs being under strain, it is difficult to see how foreign assistance in the aggregate can increase. So until we have a meaningful compromise on the budget, it is hard to see how foreign aid can increase very much, even though in my judgment we are unable to meet our international obligations as a country, given the amount of money we have to deal with.

You have cited some very compelling reasons why we need additional resources, and the cost in human terms is going to be enormous unless we and others contribute more. And you are really asking for relatively modest contributions.

Nonetheless, it is difficult to be optimistic. So within the context of the limited resources, we have to make some tough priority decisions. I think, as in past years, this committee will do the best it can to put a priority on these programs.

But I would not want you to leave thinking that we are likely to see any significant increase in foreign assistance, and you might get that impression because the people who are here are fully supportive of what you do and indeed admire very much what you do and would like to help more than we are likely to be able to.

CONTRIBUTIONS OF OTHER DONOR COUNTRIES TO CHILDREN AND REFUGEE AGENCIES

Let me ask a question first in general of all of you or any of you that wants to respond. We know what our country has been doing. What are other countries doing relative to ourselves in these areas?

UNICEF, for example, what type of response are you getting from other donor countries? And perhaps Mr. Winter as well would be able to give us a sense of these other international agencies that we contribute to. Are other countries filling in some of the gaps or are they also restrained in their contributions?

Mr. **Gautum**. Mr. Chairman, in general for foreign assistance all over the world in the 1980's it has not been a particularly good decade, as you may be aware. In fact, from the third world in the 1980's there was a net transfer of resources to the industrialized countries if you take into account all the debt payments, the repayments of interest and principal on debt.

Specifically on the programs for children, as far as UNICEF is concerned, I think we have been more fortunate than many others, in that we have continued to have a reasonable amount of growth and that a number of countries have been very generous to us. We continue to receive proportionately very significant increases from the Scandinavian countries. We have continued to receive modest increases from the U.S.

So, to some extent our budget expectations are being met. However, again everything being relative, compared to the needs of children in the world, compared to how much more we could do if we had additional resources, certainly the needs are not being met.

But we do have some good news from a number of other donors. UNICEF continues to enjoy considerable public as well as private sector support.

Mr. **McHugh**. Thank you.

Mr. Winter.

Mr. **Winter**. Yes. The U.S. for all of these organizations we are talking about in the aggregate tends to be the largest donor. On the other hand, we are a very large country, we are a very well-off country, and I think most people would expect that.

On a per capita basis we are clearly not the largest donor. There are a fair number of countries that are above us on the list. We have just recompiled the list for this year. We are about to publish our annual world refugee survey, and the U.S. has actually dropped on the list.

However, with respect to the specific emergent situation that I was explaining, it is clear that other governments do recognize that there is an emergency with the UN High Commissioner for Refugees and others and are starting to respond to it. UNHCR just got a special $15 million appropriation from the Scandinavian countries. The Federal Republic of Germany, despite all the other obligations it is seeking to accommodate right now, is in fact increasing its support for UNICEF UNHCR this year on an emergency basis, and so are a number of others.

The UN High Commissioner for Refugees about ten days ago in the New York Times said he was $150 million short this year. I doubt there is any way a big dent can be taken in a deficit of that kind without significant additional support from the U.S.

Mr. **McHugh**. Father.

Reverend **Harvey**. I would just add one other aspect to what has been said, Mr. McHugh, and that is that in addition to money sent to the foreign situation, I think we also should look at the fact that, of the 15 million refugees in the world, only a tiny minority of them are in the United States. So a lot of other nations that are hosting those refugees are really bearing the brunt of it in proportions that go far beyond our discussions today, and I think that has to be put into the scenario of how you look at your aid formulation.

Mr. **McHugh**. Mr. Lehman.

REGULATING INTER-COUNTRY ADOPTIONS

Mr. **Lehman**. Thank you, Mr. Chairman.

Once a year in South Florida, Miami, I attend sort of a family gathering, a luncheon-picnic-reception that starts around noon and goes on into the early afternoon, of families that have been involved in international adoptions. The parents are there, some single, some both parents, with their children from all over the world.

Many of these children have been brought in who are handicapped, disabled, afflicted, and some of them have been somewhat rehabilitated.

I have been with groups of parents and children in churches, in schools and other areas of the community. I have not seen a more affectionate, more joyous, more family solidity situation than I have seen with these biracial, multi-racial groups of children that have been adopted by people in South Florida.

So I am not sure I understand Father Harvey's concern about removing children from their own cultural environment when I see them so well-adjusted and so basically happy from time to time, not only individually as I meet with them, but at these events.

I am sure they have the same tensions that ordinary families do from time to time, but I do not know of any data—and if you have any, let me know—where if you adopt children from different cultures and bring them to the United States and give them the kind of care that these children receive, they have any real conflicts.

Are there any such data?

Reverend **Harvey**. I maybe created the wrong impression, because in my remarks I am not asking that international adoption be curtailed. I am merely asking that it be somewhat controlled to make sure the happy outcomes that you suggested really do happen.

I think I could get those statistics in terms of the agency placements. The private adoptions are very hard to track, Mr. Lehman, and as a result you are going to get a skewed statistic.

Even as I gave mine, I apologized. I have been told that it has been 1,000 that are in extreme situations where some exploitation has taken place and it is only estimated that between 8,000 and 10,000 private adoptions between Latin America.

But I certainly would not like to leave the committee with the idea that inter-country adoptions should be eliminated. We should try to protect them in such a way as to guarantee the kind of outcomes that you observed in Southern Florida.

Mr. LEHMAN. Even across cultural lines?

Reverend HARVEY. Even across cultural lines.

REFUGEE CAMPS

Mr. LEHMAN. And the only other fact I would like to bring out, Mr. Chairman, is that I think one of the overriding concerns is what is known as compassion fatigue, and I think that is a real problem now, not only for the people that are homeless in this country, but throughout the world.

It was brought home to me especially. Eleven years ago I went to the Far East, and I visited the refugee camps in Thailand, Hong Kong, Singapore. I talked to people about them in the Philippines and Indonesia and even in Malaysia, and it was a terrible situation.

Then I went back last November a year ago with Senator Dole on a trip to basically the same areas. And when we got to Thailand, I said to Senator Dole, I said: How are you going to Thailand and not visit a camp for refugees? So of the six people that went, Senator Dole did come with me, as well as one of the other members.

We went to the refugee camp and I saw the same children who were two and three years old ten years before, that were now teenagers and nothing had happened.

Two things I want to say. One is that when members go to Bangkok, for instance, none of them go to the refugee camps. Once you are there, you are affected. They do receive the vibrations. Besides that, it is a hell of a photo opportunity for them.

So I would try, when you find out that people are going to those areas, see that the members are scheduled to go to the refugee camps, and not just do the usual routine things, like talking about drug trafficking and things like that, because this is where they can make a difference.

One disheartening thing that I did find out at the camp that I went to after ten years was why some of these children cannot be sent to the United States, Australia, or Canada? What they told me is that the parents of these children are using the children as a lever to get themselves out. Once the children were removed, the parents would never be able to get out.

I think this is a very sad comment to make as to how, even in the camps, the adults are using the children as a last resort for themselves to be resettled to the west or some other better area of the world.

But I would strongly urge, if at all possible, that we provide the funds and do away with as much of the red tape and the bureaucracy as we can, because bringing these children over and offering them the American dream not only serves the children, but it certainly enriches the parents that bring them in here, and I think in the long run it will enrich and benefit our own country.

That is all. We have some other questions, but I think the time is about up now.

Mr. McHugh. Thank you very much, Bill.

CHILDREN IN MOZAMBIQUE

We are a little bit frustrated here because of a limitation on time. Before we adjourn, Dr. Boothby, I think you took the least amount of time, and I wonder if you could spend just another couple of minutes giving us further insight on your personal experience?

When you got to Mozambique, what did you find? What were your observations? And again, in a little bit more detail, what kinds of activities are now under way to deal with the problems which you observed?

Just take a little more time to give us a flavor of your personal experience.

Dr. Boothby. Okay. Essentially, when I arrived in Mozambique what we found was a group of 42 children who had been captured by RENAMO, the anti-government guerrilla forces there, taken to base camps, trained, and in some cases, had killed other human beings.

They since either escaped or were liberated from Renamo camps by the government troops and brought to an orphanage called Lhanguene. What was of crucial importance, of course, at this moment in time with the government, was the whole question of amnesty for these children.

Not only for these 42 children but perhaps for as many as 10,000 children elsewhere in Mozambique who had been captured by RENAMO and trained as combatants. It really is a war in which children under the age of 15 comprise the majority of Renamo combatants, especially in the southern provinces.

In discussions with the government, the whole question of amnesty hinged in some ways on whether or not one could provide some form of rehabilitation for these kids. The alternative, was to become a prisoner of war and stay in those kinds of places.

On the other side of the coin, the idea of establishing a center, which again act as magnets in these kinds of emergencies, was not a good idea. What we wanted to do was provide training and treatment for people who could then go out and work in the communities and the districts where children live in, rather than bringing children to cities, which in itself is a very disruptive experience.

So we turned Lhanguene into a training initiative. Before we began we spent quite a bit of time in the communities looking at what communities did on their own. And what we found was dance and drama and collective storytelling were the ways in which communities—the kinds of activities that they undertook on their own, that could be adopted for therapeutic purposes.

So we went back to the villages, learned what they were doing, and taught people in the Ministry of Health and elsewhere some of these things, and then took the show on the road, so to speak, and began working in districts and provinces.

The tracing program of course was very important, because it offers an alternative to orphanage use, it offers an alternative to resettlement, which is not necessarily in the best interest of the child, and it offers an alternative to international adoption, which is illegal in Mozambique and is also not often in the best interest of the child when there are families to be returned to, and when there are possibilities to create other placements within the country.

I think the other thing we have to realize about international adoption and resettlement of unattached children is that they are options that are only available for the very few. It will never be an option for the majority of children in these kinds of crises.

So our priority in Mozambique and our priority when we worked in Thailand and our priority when we worked in Central America and elsewhere is to empower families and communities and nations to take care of their own children. In many ways, this is what we have attempted to do in Mozambique, with some modest success.

Mr. McHugh. I presume that the government in Mozambique was cooperative, then, in terms of your tracing program and the efforts that you have undertaken here to reunify families? I mean, was there any resistance to this?

Dr. Boothby. Not at all. In fact, it is a government program that is assisted by U.S. funding and a U.S. organization, Save the Children. And we have the Norwegian Save the Children and the British Save the Children are also working collaboratively on this project. So it is sort of a joint international effort, run through the Ministry of Health.

We have also begun to extend the same kinds of services to refugee children in Malawi that have equal kinds of needs, both in the psychological area, but also needs to find their families and, when appropriate, return to them.

Mr. McHugh. Mr. Lehman, you had another question?

ADDRESSING LONG-TERM NEEDS OF CHILDREN

Mr. Lehman. Thank you, Mr. Chairman.

I just have one other question I want to clear up. I know as well as you do that adoption, international adoption, is not going to solve but a very, very small part of the whole problem of these children overseas that are in dire straits.

I remember a number of years ago when Mr. Obey's predecessor Mr. Long was chairman of this subcommittee and he wanted to know what happened to the children that UNICEF immunized and also did the oral rehydration. Once you did the snapshot of them, got them okay, then what happened to them?

Has UNICEF addressed the problems of these children that have been salvaged and then placed back into the situation from which they were taken and left to degenerate again? Is there any program to continue besides the one-shot program that UNICEF had at that time?

Mr. **Gautum**. Mr. Chairman, immunization and oral rehydration therapy are perhaps more well-known and publicized among the activities that UNICEF supports.

Mr. **Lehman**. That is a quick fix, but it is not a permanent solution.

Mr. **Gautum**. Exactly. They are among the more well-known and publicized of the activities that UNICEF is involved in. Those are by no means the only or in most countries even the most important things that we are involved in. UNICEF in many countries is involved in a whole series of basic services for children, including health, nutrition, women in development, problems of basic services in urban slum areas, water and sanitation.

These are all efforts aimed at the whole child, the need of the child, of which immunization and ORT are, as I said, two of the more prominent ones. So the answer to your question, Congressman Lehman, is yes, UNICEF is involved in all these situations with a number of other programs that help sustain the gains of immunization and ORT, but go beyond to other child health, nutrition, education programs.

Mr. **Lehman**. Thank you.

Mr. **McHugh**. Again, thank you very much to all of you. We will, as I said earlier, do the best we can. We will hopefully be able to provide some additional resources in the supplemental for refugees. That is something the chairman and the subcommittee are anxious to do.

But I suspect it will fall somewhat short of what we would like to do and what I am sure you feel is appropriate to do. Nonetheless, we realize this is a very important priority. And as I indicated earlier, we appreciate not just your presence here today, but, much more importantly, the work that you do on our behalf all around the world.

Thank you very much.

Tuesday, March 27, 1990.

ADMINISTRATION WITNESSES

MARK L. EDELMAN DEPUTY ADMINISTRATOR, AGENCY FOR INTERNATIONAL DEVELOPMENT.

BRAD LANGMAID, ACTING ASSISTANT ADMINISTRATOR FOR SCIENCE AND TECHNOLOGY, AGENCY FOR INTERNATIONAL DEVELOPMENT.

PRINCETON LYMAN, DIRECTOR, BUREAU FOR REFUGEE PROGRAMS, DEPARTMENT OF STATE.

JANE BECKER, DEPUTY ASSISTANT SECRETARY FOR INTERNATIONAL DEVELOPMENT AND TECHNICAL SPECIALIZED AGENCY AFFAIRS, DEPARTMENT OF STATE.

Mr. **McHugh**. Our next witnesses will be Mark Edelman of the Agency for International Development and Princeton Lyman, who is the Director of the Office of Refugee Programs at the State Department. I would appreciate both of these gentlemen joining us at the table at once.

I have a time limit of 11:45, which I am sure will not disappoint our witnesses. But I would like to have you all appear at once if you do not mind. And as always, we will include your statements in the record and ask you, if you could, to summarize them if you wish.

Mr. Edelman, do you want to go first.

Mr. Edelman's Opening Statement

Mr. **Edelman**. Thank you, Mr. Chairman. It is a pleasure for me to be here today.

Accompanying me is Brad Langmaid, who is the Acting Assistant Administrator for Science and Technology at A.I.D.

Mr. Chairman, it is worth noting that this June will mark 43 years since America launched the Marshall Plan to help rebuild war-torn Europe, and 41 years since we took that same concept and tried to apply it to less developed nations in Central and South America under President Truman's Point 4 program.

Since then the shape of America's foreign aid program has changed many times over, to the point where it may well be unrecognizable to its founders. Is that relevant today? I believe it absolutely is, because at issue is not only how to square new demands with old commitments and tight budgets, but the very aims and purposes of foreign aid.

Almost daily we hear continued calls for changing foreign aid, redefining its goals, and redirecting its aims. And the problems of children in developing nations lie right in the middle of this debate.

You have just heard testimony describing the plight of children in many developing nations, and it is indeed a sad commentary and something the United States should help to do something about. Today I would like to focus my brief remarks on A.I.D.'s vision of what we should be doing to help the children of the world. It is a vision which not only helps infants survive childbirth, but actually works to ensure that they have a safer, more productive environment to live and grow in as adults, fully contributing to the betterment of their family, their community, and indeed the world.

In order to examine that vision, though, we still have to talk a little bit about the broader goals of America's foreign aid program, because America's foreign aid program cuts across several goals, such as when and how do we use our foreign aid as a tool for humanitarian purposes, such as helping infants and mothers survive the birthing process.

Many say it is through our child survival programs, and—to a point—I agree. Because what if this child survives birth, only to be weaned on policies of hunger and sickness, poverty and despair? Has America then truly done right by this child? Have we helped that child survive, only to be thrown into a world that looks upon her as a burden, instead of as a part of the solution, doomed to a lifetime of struggle for sustenance—suffering under the misguided policies of a government that should be and could be helping instead of hindering?

What would have happened if, on the other hand, America's foreign aid had also helped to bring economic growth to this same nation? And I would note that investments in economic growth includes investments in health, nutrition, and other factors which make up a vibrant and effective nation. This investment could enable this nation to not only buy its own vaccines, but also to provide clean hospitals and prenatal care and to ensure that both mother and child are well-tended before and after birth.

Would that still be humanitarian aid? Would we not still be helping to reduce infant mortality, while increasing the chances that that child will live to be a part of a world where he will be an asset instead of a burden?

Then what happens if this same economic growth helps to provide more jobs, more income, more money in that nation, providing funds for schools and books and technical and vocational training, giving that same child not only a chance to survive, but to learn and prosper and contribute to her surroundings?

What then? Is that bad? Are we now out of the humanitarian aid business? Are we no longer talking about child survival?

When does child survival stop and enrichment begin? Is it enough just to survive when there is a way with that same money to actually help them prosper?

What if there came a time when economic growth became such that the nation became able to do some modest trading with the United States, stimulating further economic growth and more and more trade flowed between America and its new-found trade partner, bringing new prosperity to many in America as well as that developing nation?

Does that mean that our foreign aid has become a tool for our own economic interests? And if so, is that bad?

And as the trade flourishes and more people participate in that economic growth and enjoy the proceeds of greater incomes, greater hope for the future, greater hope for their children and their children's children, greater ability to make choices in their lives, what if that new prosperity helped build economic and political stability in that nation or in that region of the world?

Is there less likelihood of unrest and conflict in a nation that is beginning to prosper? Does that mean that that aid that is used to promote child survival is the same aid that helped create economic growth and has now become the same foreign aid that serves to support the strategic interests of the United States? If so, is that bad?

Now, this may strike some as a gross oversimplification of the many arguments over foreign aid, but I think it is not. The point that I have tried to make here is twofold: first, no matter what your goal for America's precious foreign aid dollar is—humanitarian, economic self-interest, security—the fact remains that economic growth in developing nations remains the tie that binds those goals with some realistic expectation of achievement.

Children are both the beneficiaries of and the future producers of the growth and development of nations. Their interests underlie our development strategy.

Second, and this is where many well-intentioned development professionals part company, these goals are not mutually exclusive. The fact is there is no such thing as aid that helps to promote economic growth that is not itself also humanitarian aid. There is no such thing as aid that helps to promote economic growth that is not itself also aid that promotes America's economic interests. And there is no such thing as aid that helps to promote economic growth that is not itself also aid that promotes political and economic stability security aid if you will.

Contrary to popular belief, we are not working at cross-purposes here. We are all singing off the same hymn sheet. We are just singing different arrangements of the same song.

We all want to dramatically lower infant mortality while increasing that child's chances for a healthy and productive life. Certainly there must be an investment in programs which decrease the rates of infant mortality. Yet at the same time we must recognize the need to go beyond child survival, to dare to dream of child prosperity, to look beyond the provision of vaccines or medicines or schooling to a day when the men, women and children, especially children, of developing nations not only can expect to survive, but to actually prosper.

So the argument here should not be over the goals of foreign aid. We all want to see better child survival, better health and literacy, and we can. We can have all of these goals and more, because if we will take care to promote economic growth while making an investment in health, literacy, and other factors which make up a vibrant and effective nation, then these goals will ultimately take care of themselves.

The vision of foreign aid of child survival then becomes not of surviving, but prospering. It can be done. The United States has done it, and more and more nations around the world are learning that they can do it, too.

We can show them how and we must show them how, for there is no greater aid for America to give than to help developing nations learn to grow, to ultimately provide for their own. That, Mr. Chairman, is my vision of child survival, a vision I hope we can all learn to share and work on in order to ensure its success.

Now I will be happy to answer any questions you may have, Mr. Chairman.

Mr. McHUGH. Thank you, Mr. Edelman.

[The prepared statement of Mr. Edelman follows:]

TESTIMONY OF THE HONORABLE MARK L. EDELMAN

DEPUTY ADMINISTRATOR

AGENCY FOR INTERNATIONAL DEVELOPMENT

BEFORE THE

HOUSE APPROPRIATIONS COMMITTEE

SUBCOMMITTEE ON FOREIGN OPERATIONS

MARCH 27, 1990

Mr. Chairman, Members of the Committee, thank you for this opportunity to discuss the approach and work of the United States Agency for International Development (A.I.D.) in attacking problems of children.

The three fundamental goals of A.I.D.'s economic development program are broad-based economic growth, human capacity development and pluralism. These goals represent our vision for the future. And, children are the future. Children are both the beneficiaries of and the future producers of the growth and development of nations. Their interests underlie our development strategy.

Sustaining the ability of a family or a society to assist its children to develop into productive members of society is key to A.I.D.'s development effort. It is not enough simply to support the provision of vaccines or medicines or schooling.

While not de-emphasizing the critical role of child survival programs, we must also look "beyond child survival". To ensure the prospects and quality of life of children:

--the economies of developing countries must grow to provide resources for health and education programs;

--family income levels must be raised and access to services and resources increased;

--health and education professionals must be appropriately trained, and such training must be institutionalized;

--donors must coordinate and work responsibly towards transition from reliance on external to domestic sources of finance;

--the private sector's capacity to communicate, finance and provide services designed for children and their families must be tapped;

--families must be provided with the information necessary to determine their children's health and educational needs; and

--families must be empowered to effectively use, and if possible to provide, the health technologies and other social services they deem appropriate.

Social progress will not be attained or sustained without economic growth and vice versa. One of the social indicators most often correlated with economic growth and development is reduced infant and child mortality. Children and adults who are sick cannot participate in the economic, political and social institutions of their communities and societies. On the other hand, without an open and economically healthy environment, even the children who survive will have nothing in which to participate. Thus, A.I.D.'s entire portfolio supports improvements in the lives of the peoples of developing countries, of whom children are the most vulnerable members.

The basis for creating and sustaining development is broad-based economic growth. Without such a growth oriented base, improvements in the prospects of children will not occur or will be short-lived. Even where there are specific technologies -- immunization, ORT, vitamin supplementation -- their continued delivery and use depends upon the resources of the society and the family.

The future of children is shaped early on by the income, education and support of their families. The family is the nexus between economic development and the next generation. Families provide the environment within which the next generation is born, sheltered, nourished and educated. Finally, it is within the family that the motivation for improving the present circumstances of and future prospects for children is strongest. Thus, everything we do to make families stronger and more economically self-reliant aids the world's children.

As we look to the future, we must try to help families increase their resources, thus enabling parents to meet their childrens' needs effectively and on a sustainable basis. Our job is to help expand the choices available to families. As choices about employment and about whether to use public or privately offered services expand, people are better able to cope with the sometimes difficult circumstances of their lives. As family income grows, their opportunities to participate in the affairs of their communities and their countries increases, as they begin to have control over their lives, personally and economically.

As we assist families create a healthy, nurturing environment for their children, we face new challenges. Children will be faced with a set of problems which have not yet been adequately addressed, whether it be acute respiratory infection, nutrient deficiencies, or the quality of education. Improvements in access to quality education will become critical to sustaining and multiplying gains already made in the health and nutrition of children. The solutions to this second generation of problems will become increasingly important as we look toward the 1990s.

A.I.D.'s approach to the achievement of sustainable broad-based growth is through policy reform, greater opportunities for the private sector, decentralization, development of human capital through education and training, and sustainable management of natural resources. Thus, through these basic approaches to development and support for some specific health interventions, A.I.D. will continue to support sustainable solutions to the problems of children and their families.

We must remember that although tremendous efforts have been made, the burden of infant and child death still weighs heavily on the families and economies of the developing world. Poverty and civil strife are major causes of these deaths. A.I.D. is ready to build on what has been learned in order to deal more effectively with the problems facing children today.

The immediate causes of death and disability among infants and young children are clear. These include diarrheal diseases, vaccine-preventable diseases such as measles, polio and neonatal tetanus and other communicable diseases such as malaria, pneumonia and other acute respiratory infections, and Acquired Immune Deficiency Syndrome (AIDS). Childhood ailments become an even greater threat when exacerbated by malnutrition, high-risk pregnancies, and lack of education. In addition, pervasive - and in some cases worsening - poverty keeps good health out of reach of too many of the world's families and the next generation they are nurturing.

A.I.D.'s experience with child survival programs of the last several years has shown that it is possible to make dramatic improvements in the prospects of the young. The challenge for the 1990s is to find ways to sustain these improvements and carry them beyond child survival. Although A.I.D. has supported child survival interventions since the early 1970s, our efforts accelerated in the mid-1980s. Since FY 1985, a total of $848 million from various funding accounts has supported child survival efforts in 60 countries.

For FY 1991, a total of $194 million has been requested for direct child survival activities. Of this total, $44 million has been requested for immunization and $42 million for diarrheal disease control. Another $36 million is proposed for nutrition activities including promotion of breastfeeding, improved weaning practices, growth monitoring and vitamin A activities. For breastfeeding programs alone, A.I.D. has requested $6 million for FY 1991. An additional $21 million of child survival resources is proposed for programs to reduce high-risk births. These programs are complemented and certainly dwarfed by the Agency's quarter billion dollar population and family planning program with its attendant benefits for the health of mothers and their children. Finally, the remaining child survival funds, some 26 percent, are being requested to fight other diseases and problems identified as important at the country level, such as pneumonia, malaria and other communicable diseases.

Beyond Survival - Growing up Healthy

Efforts to immunize children, prevent death from diarrhea, provide nutrition and space births are necessary for the survival and development of children. However, these survivors could be lost to fatal diseases like pneumonia and malaria.

Globally, some 70 percent of deaths from acute lower respiratory infection are due to pneumonia. In Honduras, Egypt and Jordan, where these infections now account for one-third of all deaths of children under age five, A.I.D.-funded projects are laying the groundwork for curbing pneumonia deaths on a large scale.

Malaria also accounts for a significant proportion of child deaths. In Africa, where the most severe form of malaria is endemic, conservative estimates put annual child deaths due to the disease at one million, making some 25 percent of all child deaths there due to malarial infection.

Through its Vector Biology and Control project, A.I.D. is improving malaria control efforts throughout the developing world by providing technical assistance and training in surveillance, data management, operations research and vector control.

As we save young lives with our proven interventions, a new specter is emerging on the horizon. The future of children is being threatened by AIDS. An increasing number of infant and child deaths are attributed to perinatal infection with the human immunodeficiency virus (HIV), which causes AIDS. In Uganda, for example, current projections suggest that the virus could increase infant mortality in Kampala from 5 percent to 42 percent over current levels. A.I.D. programs designed to prevent and control AIDS also contribute to prevention of pediatric AIDS and therefore to the survival of children. In FY 1991, A.I.D. plans to support the World Health Organization's Global Program on AIDS at a level of $21 million and to provide an equivalent amount in bilateral support. Some of the threat of AIDS to children is indirect. In Uganda, parental death from AIDS is a major contributor to its orphan population.

Consistent with our Congressional mandate to help the orphans of civil strife, A.I.D. is assisting the world's most defenseless. In many cases, we must solve these problems family by family. For example, last year in Mozambique

--over one thousand children were reunited with relatives and given food, clothing and educational supplies,

--approximately 540 displaced and traumatized children underwent treatment and counselling, and

--another 2,300 children living in orphanages or with substitute families received food and household goods.

Similar assistance is being provided in Ethiopia, Madagascar and Uganda. Through programs run by local and international non-governmental organizations and host-country governments, orphans are being fed, resettled, counselled, and provided health care. Orphanages are being built, remodeled and supplied with mattresses, blankets, cups, plates and hoes. Orphanage workers and government officials are being trained in child care, family tracing and resettlement, and in the screening and treatment of children traumatized by war and the loss of their families.

Over one-third of the FY 1990 $3 million Agency-wide development assistance funding for aid to orphans is already programmed for Mozambique and Uganda. OFDA's five hundred thousand dollar level is scheduled to be split among Ethiopia, Angola, Mozambique and Uganda.

A.I.D. will continue to respond to the needs of these children, but this must be done within the context of broad-based sustained development that can provide the necessary resource base to support the next generation, even in times of crisis.

Educating the Next Generation

The key to such self-sufficiency will be education. Raising the education levels, especially for girls and women, is among the most powerful and cost-effective means of supporting reductions in family poverty, improvements in child survival and family health, full economic and political participation and informed choice in all aspects of women's lives. The graduates of the child survival revolution can only become productive members of modern society with a basic education. As more children survive to schooling age, the quality and efficiency of educational systems must improve to meet their needs, increasing the demands on an already over-burdened human and physical infrastructure. Countries need to use education resources more efficiently, to make better use of family and community resources for education, to use instructional technology to moderate costs and reach isolated communities, and to resolve the problems of access, quality and relevance which limit the participation of girls, and poor and rural children. Countries facing these new challenges will also need to find ways to sustain achievements already made. We can help them. A.I.D. has been a leader in international assistance to education for more than three decades, and our emphasis on basic education expansion and reform is not new.

With the conclusion of the World Conference on Education For All a renewed sense of the importance of basic education has emerged. A.I.D. wants to continue to play a leading role in donor support for basic education. This does not mean that we as an Agency are able to carry a heavier financial burden. A.I.D. will seek, instead, to combine its resources with those of other donors and the host country to help address the growing needs of educating children worldwide. Currently, we support basic education programs in over 25 countries, with activities ranging from policy reform programs in Mali and Pakistan, to a bilingual education project in Guatemala.

A.I.D. obligates approximately $135 million annually for basic education programs designed to support country efforts to expand and improve the quality of their primary and secondary schooling systems.

The Challenge for the 1990s

We are all aware that many families in the developing world still lack access to the resources and services necessary to improve their own lives and those of their children. However, the gains already made are impressive and they will have a lasting effect since improvements in education, health, family planning and nutrition tend to be passed on from generation to generation. However, we must continue to build on these gains and maintain the momentum achieved in service delivery, while working harder to achieve sustainability through increases in national and family resources, derived from broad-based economic growth.

Beyond the survival and education of the next generation, we must provide an environment that can allow and sustain growth, development and participation in society. The establishment of a healthy economic and social environment in developing countries is the primary objective of our foreign assistance. This means:

- agricultural research to ensure adequate food,

-open markets and private enterprise to ensure adequate jobs,

-democratic values and institutions to allow the participation of all people,

-economic policies to encourage trade and investment, and

-wise management of natural resources to ensure sustained growth.

Remarkable strides have been made. Our record is an impressive one, one that I am committed to continue with the support of the U.S. Congress and the American people.

Mr. McHugh. Why do we not take Mr. Lyman before we take questions, so as to be sure to get his statement in.

AMBASSADOR LYMAN'S OPENING STATEMENT

Ambassador Lyman. Thank you, Mr. Chairman.

You have been discussing this morning the plight of children and I would just start by noting that some half of the world's 15 million refugees are children and women, and children make up about 70 percent, and they are subject to special vulnerabilities which have been recognized and discussed this morning: statelessness, physical violence, malnutrition, emotional trauma faced by children through separation and violence, et cetera.

These have become much more a focus of the UN High Commissioner for Refugees and Special Programs. We have supported that strongly with our contract with the Center for Disease Control in Atlanta, which periodically monitors the nutritional level of refugees. Special feeding, supplementary and therapeutic feeding programs have been introduced. Counseling for the victims of violence is supported strongly by the United States in Southeast Asia.

And we have pressed, and at last successfully, for the formation of committees on unaccompanied minors in each of the first asylum countries in Southeast Asia. There have been more education programs.

We continue to provide special programs for Amerasians coming to the United States and other refugees coming to the United States, especially treating the special needs of children.

With all of that—and we will continue to support it—the problem of refugees is growing, Mr. Chairman, and the demands on the international community are increasing. I would like to address that also, and I know it came up in your discussion in the previous session.

First I would like to address the international community's response in general. In fact, the contributions of the donor community as a whole in cash and kind to the international refugee organizations over the past few years have either remained the same or increased, at least in nominal terms. They have not decreased.

For example, the programs of the UNHCR have been fully funded from the time in 1983 when the budget was $398 million through 1988, when it was $545 million. Moreover, 85 percent of the cash and food requirements of these organizations continues to be contributed by the same ten governments and the European Community, and in that group the U.S. has remained the leading contributor.

What has changed, however, is the number of conflict and refugee victims, and particularly in countries which are themselves the poorest. In 1985 we were addressing the needs of ten million refugees; in 1988 over twelve million. Today we are talking about 15 million refugees.

Second, on the positive side but adding to funding needs, there is greater access to conflict victims today, which allows for more protection and more humane treatment.

And third, there have been opportunities for solutions to refugee situations in several parts of the world, but those too are more costly.

As an example of the increasing numbers, we have the recent situation out of Liberia, which has produced over 140,000 refugees into Cote d'Ivoire and Guinea. We have the increased number of boat people coming from Vietnam, and we have a continuing influx of Mozambiquans into neighboring countries. This year 70,000 new arrivals from Afghanistan arrived in Pakistan.

On the opportunities side, there has been the repatriation of 42,000 Namibians, 11,000 Salvadorans, and 47,000 Burundians. And in spite of all the terrible tragedies taking place in the Horn of Africa, there is in fact the prospect of settling finally the several hundred thousand Ethiopian refugees who have been in Somalia for more than a decade.

UNHCR

But all of these take extra special programs and additional costs. The full force of this funding crisis, rising demands against limited international capability, hit in 1989. For the first time, UNHCR was forced to carry over a deficit from one year to the next, and the same was true on a smaller scale for the ICRC. This was in spite of a U.S. contribution in that year to UNHCR of $125 million, $14 million more than any year since 1985.

Recognizing the seriousness of this, the Executive Committee of the UNHCR, that is composed of major government members, set up a Working Group which has, in conjunction with UNHCR, been making an exhaustive review of the UNHCR budget, its needs, and its priorities. And until that review is complete, UNHCR must hold its expenses to last year's level.

This examination is nearly complete and the results will be the subject of an extraordinary meeting of the Executive Committee in June. But we have already learned a great deal. We now have a much better understanding of UNHCR's budget and, frankly, of the costs of those added mandates that we and other members of the EXCOM have pressed upon UNHCR.

Second, we are going to have to face some very hard choices. For example, in recent years the UNHCR, with the Executive Committee's encouragement, has extended its concern for refugees to mobilizing and in some cases contributing resources for longer term development projects in areas where refugees have made a major impact. Is this an appropriate role for UNHCR or should this be more the province of UNDP, the World Bank, and other agencies? And will they pick up this particular mandate related to refugees?

In providing protection and care and maintenance, UNHCR has in recent years gradually developed more programs of education, income generation, and special protection for vulnerable groups. This has been particularly important for women and children, who are the special focus of this hearing. How far should UNHCR go in this direction when its resources are constrained?

A third issue: In Southeast Asia, UNHCR has been given a mandate that extends in part to the protection of people not deemed to be refugees. How far should we expect UNHCR to move in this direction when resources are so constrained?

FUNDING FOR REFUGEE ADMISSIONS AND ASSISTANCE

As we go through this very difficult budget process—and I might say the same process in one way or another is going on in most refugee relief agencies today—we have tried to be alert to not jeopardizing life-sustaining or other vital programs. Thus, the President recently approved a drawdown of $25 million in emergency funds to assist such life-threatening programs or other vital programs during this budget crisis period. We have been particularly attentive to the situation in Ethiopia and Malawi and to the new situation developing in Liberia.

Looking ahead and without trying to anticipate the outcome of the extraordinary meeting this June, it is clear that the levels of expenditures projected for UNHCR in 1990 so far—and I would add this is true for most other refugee agencies—will not be sufficient to meet the full range of responsibilities which we have given to these agencies.

For our part in presenting to the Congress a supplemental request for $70 million to cover our admissions shortfall, we have freed up the emergency fund which we anticipate allocating to these additional assistance needs. Moreover, in 1991, as you know from our budget submission, we are proposing a $46 million increase in our level for refugee assistance in fiscal year 1991 over '90, as well as replenishment of the emergency account.

Nevertheless, the answer is not simply for the U.S. to do more. As I noted before, the UNHCR budget and for most of the other agencies has relied on the same ten donors and the EC for many years. Others must do more, and we must be painstaking in our examination of priorities and of added mandates which we give to these agencies.

Finally, we have to have the flexibility to respond to opportunities that arise for durable solutions, such as the ones I mentioned.

I will not go into detail on the '91 budget, but I am happy to answer questions on it. Let me just make one quick remark on the admissions part of our budget. We had two major breakthroughs this year. We have been able to set up a system for processing Soviet refugees directly in Moscow. That will save us some $40 million in admissions costs over this year, and that is reflected in our lower request for admissions next year, even though we are anticipating the same number.

Second is we now have access to the former re-education prisoners in Vietnam. We are now able to bring them out. We expect to have 7,000 joining their families and loved ones in the United States this year and project 10,000 for next year. These are highlights of the admissions program. There are other details which I can get into.

Mr. Chairman, let me just summarize by saying we face a growing problem in the refugee area. We face limits on the amount of resources which we and others can put to this task. We do have to do more, but we will face some hard choices in terms of priorities and allocations of our resources between pressing needs.

Thank you very much.

[The prepared statement of Ambassador Lyman follows:]

STATEMENT
OF
AMBASSADOR PRINCETON N. LYMAN
DIRECTOR, BUREAU FOR REFUGEE PROGRAMS
DEPARTMENT OF STATE
BEFORE THE
SUBCOMMITTEE OF FOREIGN OPERATIONS, EXPORT FINANCING AND RELATED PROGRAMS

Thank you Mr. Chairman.

Little more than a week ago, I had the opportunity to testify before this Committee on the Administration's request for FY 1990 supplemental appropriations for the refugee program. Today, I would like to continue that presentation with the details of the Administration's request for FY 1991 appropriations for the refugee program.

Before going over those details, however, I would like to discuss in general terms some of the problems and some of the trends we are facing in dealing with the world's refugees which I believe will face us throughout the decade of the nineties.

First, I would like to address the international community's response as a whole to the needs of refugees worldwide. Recently, there has been a lot of attention focused on the international community's responses to the needs of refugees and conflict victims.

Government contributions in cash and in kind (primarily food commodities) to the international refugee organizations over the past few years either have remained the same or have increased; they have not decreased. For example, programs of the United Nations High Commissioner for Refugees (UNHCR) have been fully funded during the period from 1983, when UNHCR's budget was $398 million, through 1988 when it was $545 million. Furthermore, over 85% of the cash and food requirements of these organizations continues to be contributed by the same ten governments and the European Economic Community (EEC). Among the donor governments, the U.S. has remained the leading contributor.

What has changed dramatically, however, is the substantial number of refugees and conflict victims in countries which themselves are among the poorest. Thus in 1988 we were addressing the needs of 12.6 million refugees. Today the figure is 15 million. Second, on the positive side but adding to international funding needs, there is greater access to conflict victims today allowing for better protection and more humane treatment. Third, there have been new opportunities for solutions to refugee situations in several parts of the world, which may have been welcome but, again, costly. As examples of the increased numbers of refugees and the generation of new needs in the past year, we have witnessed the flight of 140,000 Liberians into Guinea and Cote d'Ivoire this year; the flight of refugees and displaced persons to and from Senegal and Mauritania last year; the increased number of new Vietnamese boat people; the continued exodus of a monthly average of

15,000 Mozambicans into neighboring countries, especially Malawi; and up to 70,000 new arrivals of Afghan refugees in Pakistan. These are some of the increased numbers and needs which have emerged in the past two years alone.

On the opportunities side, there have been the repatriations of 42,000 Namibians, 11,000 Salvadorans and 47,000 Burundians. In spite of the other tragedies which loom in the Horn of Africa, we are surprisingly close to being able to resettle or repatriate most of the Ethiopian refugees in Somalia, many of whom have been receiving assistance for a decade. There has been greater access to Amerasians and reeducation center detainees in Vietnam, and greater access by the International Committee of the Red Cross (ICRC) to political prisoners in a number of countries.

The combination of needs and opportunities has severely strained the budgets of these organizations and of the traditional ten government donors and the EEC.

The full force of this funding crisis emerged at the close of 1989. For the first time, UNHCR was forced to carry over a deficit into the next year. The same was true, though on a smaller scale for ICRC. This, in spite of a U.S. contribution to UNHCR of $125 million, $14 million more than in any year since FY 1985. Recognizing the seriousness of this development, the Executive Committee (EXCOM) of the UNHCR, set up a Working Group which has, in conjunction with UNHCR management, been making an exhaustive review of the UNHCR budget and its various components. Until that review is completed, UNHCR has been asked to maintain its spending at an annual rate equal to last year's and below what UNHCR originally projected as its needs this year.

This examination is nearly complete and the results will form the basis for discussion at the extraordinary meeting of the Executive Committee this June. We have learned a great deal from this review. Donors now have a far better understanding of UNHCR's budget process and -- to be frank -- of the costs of programs and extensions of the UNHCR mandate which the EXCOM or its individual members have called for in recent years. All of us -- the donor community, the host countries, and UNHCR -- will now face some hard choices and decisions. For example, in recent years, UNHCR -- with EXCOM encouragement -- has extended its concern for refugees to mobilizing and in some cases contributing resources for longer term development projects in areas impacted by refugees. Is this an appropriate role for UNHCR or should this be more the province of the United Nations Development Fund (UNDP), the World Bank and other development agencies? In providing protection and care and maintenance for refugee populations, UNHCR has gradually developed more programs of education, income generation, and special protection for particularly vulnerable groups. This particularly has benefitted women and children who are a special focus of this hearing. How far should UNHCR go in these directions in a time of resource constraints? In Southeast Asia, UNHCR has been given a mandate that extends in part to the protection of those deemed not to be refugees. How far should we expect UNHCR to be able to move in this direction, and will the funds be there to enable it to undertake this task properly?

As this process unfolds, we have been especially alert that life-sustaining and other vital programs not be jeopardized. Furthermore, it has been essential that UNHCR be able to respond to new emergencies, or opportunities, when they arise. Thus, the President recently approved a drawdown of $25 million in emergency funds to assist in life-sustaining programs that were in jeopardy and for new emergencies. In the former category, we have been particularly attentive to the needs in Ethiopia and Malawi. In the latter category, rapid action was needed to assist the Liberian refugees. The U.S. is the first to respond to UNHCR's special appeal for this situation.

Looking ahead, and without trying to anticipate the outcome of the extraordinary meeting of the UNHCR Executive Committee, it is clear that the levels of expenditures projected for UNHCR in 1990 to date -- and I would add the other major refugee agencies as well, which are going through similar if less formal exercises -- will not be sufficient to meet the full range of responsibilties which we have given to these agencies.

For our part, in presenting to the Congress the supplemental budget request of $70 million to cover our full admissions costs, we have made it possible to plan on use of the President's Emergency Refugee and Migration Assistance Fund for urgent assistance purposes. As I have indicated, the President has already authorized use of half that Fund for these purposes.

Nevertheless, the answer is not simply for the U.S. to do more. As I noted earlier, the budget of UNHCR, and again it holds true largely for the other international organizations that provide refugee assistance, has relied on the same ten donors and the EC for many years. Others must do more. Furthermore, we must be painstaking in our examination of priorities and of any added mandates which we give to these agencies. Finally, we must have the flexibility to respond to opportunities that arise for durable solutions in refugee situations.

International Refugee Assistance

For FY 1991 we are requesting a total of $215.2 million to support international refugee assistance efforts overseas. This is an increase of $46.6 million over the FY 1990 appropriated level for international refugee assistance activities. In addition we are requesting a $25 million replenishment of the Emergency Refugee and Migration Assistance Fund. This request level supports our belief that all donors -- including ourselves -- must do more to meet the needs of refugees worldwide. This request proposes $39 million for East Asia, $75 million for Africa, $88 million for the Near East, and $13 million for Central America, all increases over FY 1990. Increased funds will be provided to the UNHCR, the ICRC, the United Nations Border Relief Operation, and the UN Relief and Works Agency for Palestine Refugees in the Near East, as well as to the United Israel Appeal in support of the resettlement of refugees in Israel. While we recognize that this increase is modest in relation to the great increase in the arrivals of Soviet Jews in that country, the proposed USG contribution -- $30 million in FY 1991 -- represents only a small part of the total budget of the United Israel Appeal. We also recognize that this program benefits from an extraordinary worldwide private funding effort. In addition, we are requesting $5.7 for the International Organization for Migration which continues to play an essential role in assisting refugees and migrants around the world.

These assistance funds, in combination with our continued generous refugee admissions policy, will help maintain the traditional U.S. humanitarian leadership role in the international community.

U.S. Refugee Admissions

In our admissions program we have achieved several milestones in FY 1990. One was the establishment of a far more efficient and effective system for processing Soviet migrants. This fiscal year, 50,000 will move from the Soviet Union as refugees, and another 10,000 to 12,000 will move as immigrants and parolees. The second milestone was in reaching an agreement with the Government of Vietnam to be able to process those who had served long years in reeducation camps. This fiscal year, ending September 30, we estimate that 7,000 former reeducation center detainees will join their families and loved ones in the United States after years of separation.

The FY 1991 request for funds to be used in carrying out our refugee admissions program totals $185.2 million. This request level, I am pleased to report, is a decrease from the FY 1990 level -- assuming the Administration's request for supplemental appropriations in the amount of $70 million is granted in full. This decrease, as you know, is a result of the decision to process Soviet refugee applicants in Moscow rather than in Rome and Vienna which will save millions of dollars in U.S.-funded care and maintenance costs. Under the current plan we hope to have moved the last Soviet refugees from Vienna and Rome to the U.S. by the end of May.

The funds requested to carry out our admissions program in FY 1991 are required to finance the admission of 110,000 fully funded refugees in FY 1991. This budget currently makes no provision for any of the unfunded numbers that have been utilized in recent years. We would welcome the opportunity to work in conjunction with the private sector to see what would be possible again in FY 1991. Allow me here to express again our appreciation and sincere gratitude for the private sector response we have received in support of this effort this year.

The actual admissions levels will be set later this year by the President in consultation with the Congress, as provided in the Refugee Act. For budget purposes, we have estimated 110,000 funded refugee admissions for FY 1991. Of these, 23,000 are projected from East Asia first asylum countries; 29,000 from Vietnam under the various orderly departure programs; 40,000 from the Soviet Union; 5,500 from Eastern Europe; 6,000 from the Near East and South Asia; 3,500 from the Western Hemisphere; and 3,000 from Africa.

Of the 29,000 projected admissions under the orderly departure programs, 14,000 are direct departures from Vietnam and 15,000 are Amerasian. This level for Amerasians together with what we accomplished in FY 1989 and expect to accomplish in FY 1990 should go a long way toward achieving the goal of admitting all those Amerasian children and family members who wish to come to the United States. As of this month, a total of more than 33,000 individuals had left Vietnam since the beginning of the Amerasian program. By the end of this fiscal year, we expect that total will approach 45,000 -- 32,000 of whom will have left Vietman since the enactment of special Amerasian immigration legislation in 1987.

I would like to call your attention to the projected level of admissions for Soviets. We want to be able to expand opportunities for Soviet refugees to come to the U.S. in FY 1991 as our fair share of the number pressing to leave there. Therefore, the Administration places high priority on the pending proposal for special immigrant legislation which could provide for the admission of a substantial number of Soviets beyond the funded number of refugees and normal number of immigrants. The total number of Soviets coming to the U.S. in FY 1991 should thus exceed the number of more than 60,000 in FY 1990.

Administrative Expenses

This request includes $8,528,000 for the administrative expenses of the Bureau for Refugee Programs. This is less than 2 percent of our total program request. These funds are required to finance the salaries and operating costs associated with a staff of 107 permanent positions in Washington and overseas -- the same level as last year. Much of these funds are directly associated with monitoring the condition of refugees and the effective use of U.S. Government funds.

Conclusion

All of us are faced with making difficult budget decisions, none of which are more painful than those which affect the well being and future of other human beings. In formulating this request, we have tried to meet the most urgent needs of those who need our help the most as well as to meet the other fundamental humanitarian objectives of the Migration and Refugee Assistance Act of 1962 and the Refugee Act of 1980.

Mr. McHugh. Thank you very much.

We have about ten minutes left and Mr. Porter has not had a chance to ask questions. So why do I not recognize you, John, at this point.

AID TO STATES FOR RESETTLING REFUGEES

Mr. Porter. Thank you, Mr. Chairman.

Ambassador Lyman, I understand that we are now down to paying 80 percent of four months cash and medical assistance to the States for refugee programs. Two years ago we were providing 24 months. A few months ago we were fighting over whether that should be lowered to 15 months. Now we are down to four months.

It seems to me that we are not talking about making tough choices. We are copping out on the tough choices. We are not giving the kind of aid that we ought to be giving to resettle people throughout our country.

Mr. Chairman, I would like to submit for the record a letter from the National Conference of State Legislatures addressed to me, discussing this problem.

[The information follows:]

National Conference of State Legislatures

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House Minority Leader
Illinois
President, NCSL

Patrick J. O'Donnell
Clerk of the Legislature
Nebraska
Staff Chair, NCSL

William T. Pound
Executive Director

March 21, 1990

The Honorable John Edward Porter
U.S. House of Representatives
Washington, DC 20515

Dear Representative Porter:

On behalf of the National Conference of State Legislatures, I am writing to urge your support for a supplemental appropriation of $52 million for refugee cash and medical assistance.

The FY90 Appropriations Conference Report on Labor, Health and Human Services and Education, on page 28, specifies that "...the period of reimbursement for cash and medical assistance [should] not fall below 12 months." Recently, state refugee coordinators were informed by the Family Support Administration of the U.S. Department of Health and Human Services that only 80% of four months of cash and medical assistance could be provided due to a funding shortfall.

This shortfall must be resolved expeditiously. Its causes are obvious to states. First, the Administration continues to retreat from its responsibility to pay for a reasonable period of resettlement costs. In FY89, the cash and medical assistance program for categorical refugees was cut from twenty-four to four months. Secondly, the FY90 appropriation, to everyone's knowledge, failed to account for an authorized increase, from 84,000 to 125,000, in the refugee admissions ceiling. As long as the federal government continues to make foreign policy-related decisions, such as refugee resettlement determinations, it should pay for them.

I am further inclined to seek a supplemental appropriation based on recent testimony delivered by the Acting Assistant Secretary of the Family Support Administration. That

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testimony concludes: "...While the number of months of state **reimbursement** for categorical refugees is significantly **reduced from** past year levels, this had no effect on an individual's basic program benefits. Reimbursement of state **costs** for cash and medical benefits provided to categorically eligible refugees will be put more on a par with states regular AFDC and Medicaid program obligations." These obligations, particularly Medicaid, have been major contributing factors in establishing the very tenuous fiscal conditions found today in most states.

NCSL believes that an international and domestic assistance program for individuals compelled to flee their native lands is essential. Such programs are costly despite their necessity. The State Department, when submitting its FY90 budget, admitted that it would require a supplemental appropriation to process the increased number of refugee admissions from 84,000 to 125,000 when the admissions ceiling was raised. In fact, the State Department has requested a $70 million supplemental appropriation --- but none of this is for domestic resettlement assistance. There should be a corresponding increase in domestic assistance to refugees to sustain their adjustment to the United States and help them become self-sufficient and productive. Transferring the federal responsibility for these services **creates a fiscal burden on states and a limitation on the availability of critical employment, education and social services.** I urge you to place the FY90 appropriations needs for the domestic refugee resettlement program on the same footing as that accorded the decisions to permit processing, transportation and entry of refugees.

Thank you for your consideration.

Sincerely,

Eddie Bernice Johnson

Eddie Bernice Johnson
Texas State Senate
Chair, NCSL Committee on Human Services

Mr. PORTER. The States are simply as strapped as they can be and unable to come up with additional funds. We have nothing in the supplemental, not one single penny, to aid them in resettling refugees in the United States. It seems to me that it is incredibly reproachful, that the United States should not be providing any money, and apparently there was none requested by the White House. The States are really called upon to bear huge resettlement costs that we ought to be paying.

For most of the eighties, there was a trickle of people coming in from the Soviet Union and our resources were committed, as they should have been, to people coming in from Southeast Asia and other points around the globe.

Now, with something happening that we had urged and fought for for years and years and years, the Soviet Union finally relents, people are allowed out, and we embarrass ourselves by not providing the kinds of funding to get them to our country or wherever they are going, nor to resettle them. This embarrassment has begun in Rome and now it has reached the United States.

So it seems to me, Mr. Ambassador, that we are not living up to our responsibilities at all. I do not know how we can expect the States to bear these costs, and I am appalled that the supplemental did not contain at least $50 million to help in resettlement costs. Four months is ridiculous, it really is ridiculous.

I guess that is not a question.

Ambassador LYMAN. I could only make a brief comment. I understand the problem we have dealt with. We have been in discussion with the governors and States and, as you know, it is part of a different budget that you are talking about, the Health and Human Services ORR budget.

The compensation for the States and local governments on AFDC has gone down to four months. It has not gone down that low for other elements of it. And this does put a greater burden on the State and local governments for refugees who need access to that kind of welfare payment for longer periods of time.

There has been an effort in ORR, and I do not want to speak for them, but to work with the States and the voluntary agencies with the matching grant program and other programs to get refugees launched into employment as soon as possible, and a number of promising efforts are going on on that. But I again would refer you more to that agency for details.

But your point is well taken.

Mr. PORTER. Well, just to tip off my chairman here and staff, I have looked at the first draft of the supplemental. I find in it $50 million for low income energy assistance, which we already put $1.3 billion into this year. And it seems to me that $50 million is much, much better spent by sending the money to the States and helping them to resettle refugees who are coming in in large numbers and they are not getting the assistance they need. And I would hope I could see the support of my chairman in moving that money to that purpose, or other money.

WORLD HEALTH ORGANIZATION GLOBAL PROGRAM ON AIDS

Ambassador Edelman, a few weeks ago Dr. Jonathan Mann resigned as head of the World Health Organization's global program on AIDS. Will his resignation have an adverse impact on the program? Let me ask that first. What are your thoughts?

Mr. EDELMAN. Let me first of all say I think I share the implied enthusiasm for Dr. Mann's work. I first met him when I was traveling in Zaire, I think it was 1985, and I have tried to snare him whenever he was in town just to talk to him.

Dr. Mann is a unique fellow who not only speaks French, but he speaks lay-man's English, instead of in internationalese or medicalese. He always had clear priorities. It was easy to understand what he was talking about, and he probably has done more than any other human being on this earth to help get a handle on the scourge of AIDS.

I do not know his replacement, but maybe Mr. Langmaid wishes to answer, because he has been working very closely with Dr. Mann, with the World Health Organization, and with this program.

I personally think it is tragic that Dr. Mann decided to resign. I do not think he actually resigned but it was the end of his tour and he simply decided not to continue. Whichever it is, he is an extremely gifted fellow who is always welcome in my office. As I said, I tried to find out when he was in town and would go out of my way to get him to come by, and encouraged others to join us, too, because of his vision, and his ability to talk about the problem of AIDS.

The AIDS problem, as much as anything else, is an education problem—in educating people as to what the problem is and educating governments and people as to what they need to do. His skills were unique in that he was able to educate people in an easy to understand language and the data was right in his head.

I fear, but do not know, that some of Dr. Mann's effectiveness may be lost. But if Mr. Langmaid might comment, because he knows this cast of characters much better than I.

Mr. LANGMAID. Yes, I believe that Dr. Michael Merson, who is a U.S. Public Health Service officer now assigned to WHO, will be asked to take on that task for the next three or four months, while a more thorough search goes on for a permanent replacement.

Mike Merson is well known to us. He has been heading the diarrheal disease program at WHO, which is part of our overall child survival effort. He is a very skilled international public servant, as well as a very skilled Public Health Officer.

Jonathan left behind a strong staff. A key issue will be whether and where that staff is retained. I have every confidence that Mike will want to retain that staff.

I think there are at least three issues that need attention. Dr. Mann left in the middle of a reorganization program at GPA. It will be essential that that task be completed in a timely fashion.

He left in the middle of a decentralization process whereby a good deal of program implementation responsibility is shifting to the regional offices of WHO. I think a number of the donors to the GPA program have considerable concern about the effectiveness of that initiative and we will be paying close attention to that over the coming months, as Dr. Mersin takes over.

Lastly, Dr. Mann had initiated a number of very interesting initiatives with the PVO community. I think this may be the first time who is involving the PVO's in their programs in a direct fashion. That is also a key issue for us to look at.

The doners to the GPA will be meeting at the end of April. I represent the U.S. Government at the GPA meetings. I also expect to meet with Dr. Merson next week when he is in Washington. These are the issues that will be on our agenda, to ensure that business continues with the same kind of leadership that Dr. Mann gave it.

Mr. PORTER. Let me urge you to put one other issue on that agenda. The WHO's AIDS program was really centrally managed by Dr. Mann, and it was centrally managed by Dr. Mann because WHO's regional offices were not as strong as they should have been.

There is some concern that these regional offices, including the one in Africa, are really not competent to manage this vital program and that you must have somebody like Dr. Mann who could manage it at the top. What are your thoughts about that?

Mr. LANGMAID. That has been an ongoing concern of ours and was a specific concern of Dr. Mann, as he approached the issue of decentralization to the Africa Bureau.

Mr. PORTER. Some people think that is the reason he resigned.

Mr. LANGMAID. I think it was one of his concerns. It was a very frustrating environment for him to operate in, given the obvious needs in the African region in the AIDS area. I do not think it was a concern vis a vis some of the other regional offices. Clearly the EUR office and the PAHO office are outstanding organizations and are providing very effective support for AIDS.

But there has been concern about the technical skills available at some of the regional offices and this issue will clearly be part of our discussions with Dr. Merson when he is in here.

Mr. PORTER. If the United States is to continue to provide support for the GPA through WHO, we would be very greatly concerned that that money is well spent and not wasted, and that Dr. Mann's successor understands the importance of seeing that it goes for the purposes for which it is being appropriated.

Mr. LANGMAID. We agree with you completely.

ISRAELI HOUSING GUARANTEES

Mr. PORTER. Let me ask a question on the Israeli housing situation for anyone who want to answer it. I understand that there is a proposed two percent up-front charge and a five-tenths percent continuing charge made against all housing credits to hire architects-engineers and to monitor the program.

These charges, I understand, would amount to about $2 million annually and they would be charged against the housing program to the Israeli government. Do we really need to have a $2 million charge to monitor the program in such an advanced country? Why is this necessary?

Mr. EDELMAN. Let me say, Mr. Porter, that I do not know the details on those charges and I will be glad to look into it. Offhand $2 million strikes me, I must say, the same way it strikes you.

I am aware of legisltaive proposals that there be no charges. This would mean that the cost-burden of monitoring the program would rest on all of the other borrowers. We would like to levy a fair charge, so that the Israeli program bears its portion of the costs.

As I understand it, there is a general agreement in principle but I am quite willing to look into the issue for you.

[The information follows:]

First, fees are the source of operating expense funds for A.I.D., which manages the Housing Guaranty Program worldwide. If the fees are waived, other countries will in effect assume the expense of management of the Israel program. Also, A.I.D. will be assuming an unprecedented increase in its level of contingent liability, without any increase in its income to compensate for this liability. A proposal to waive the fees could have a serious negative impact on the Program in the eyes of other developing nations, who are following the relatively heavy coverage of this matter in the press.

Second, while A.I.D. would not manage the Housing Guaranty Program in Israel exactly the way it manages programs in other countries, some A.I.D. involvement is necessary and desirable. In the 1970's, A.I.D. typically did provide oversight and analysis, including a comprehensive annual review of the Israel HG program. This process came to be regarded as a very positive exercise by the Israelis and resulted in some important changes in Israel housing policy, such as those affecting housing maintenance and adjusting mortgages for inflation, know as indexing. We believe the new program can and should operate under similar criteria.

Mr. PORTER. The subcommittee is marking up in 55 minutes.

Thank you, Mr. Chairman.

Mr. MCHUGH. Thank you, Mr. Porter.

It is now almost ten to 12:00 and I have a whole series of questions, which obviously I will not have time to ask, but perhaps I can submit to you.

It is my understanding from staff on the housing question that the authorizing legislation permits A.I.D. to charge up to a certain percentage on the housing guarantees, but A.I.D. is not required to charge those fees, depending upon the circumstances.

And in the case of the Israeli housing guarantees, because we are not providing the technical assistance that we often provide with housing guarantees in addition to the guarantees themselves, A.I.D. may choose not to charge the fees that it could charge under the authorizing legislation. I understand it, in the Israeli program we are not going to provide the technical assistance, so these overhead costs therefore will not be incurred as they usually are in other programs.

In any event, you will look at that, as you say.

ADMINISTRATION'S BUDGET REQUEST FOR UNICEF

Mr. Edelman, I must say I agree with what you strongly suggested in your opening statement, that economic growth is very important to growth and the development of poor people, and so I have no quarrel with that. The problem is that as we look at the details of your budget submission there are some proposed reductions in programs which are designed to deal with the immediate problem.

I think, as you said, there is no conflict in principle between the long-term economic growth and the economic reforms that are needed and the immediate humanitarian response that we have traditionally had to the problems that children, for example, incur in these poor countries.

The problem is the budget submission proposes reductions in some of the programs which are designed to meet the immediate need and, while I do not have a quarrel with your initiative in the area of policy reform—I think you are right about that; it is important in the long run that these countries adopt sound economic principles, not only in the interest of sound economic principles, but in the interest of their own people's growth and development.

But unfortunately, if we in the meantime curtail our ability to respond to the immediate life-threatening circumstances that many of the children and poor people have in these countries, we are obviously going to undercut our traditional response.

Now, one of the programs we talked about in the prior panel's discussion was UNICEF. This does not fall under your bailiwick, but it is an example of a concern I am sure our subcommittee will have.

Ms. Becker is here, I think, Deputy Assistant Secretary for International Organizations and Programs, and perhaps she would want to try to respond to this. But I think the subcommittee wonders why there has been a cut or a proposed reduction of $15 million from the amount that was appropriated last year for UNICEF.

So far as we can tell—and certainly the testimony that we have had at the prior panel would suggest that—the problems are no less. Indeed, in some cases they are worse. UNICEF, I think most folks would agree, hopefully the Administration agrees, that UNICEF plays an important role in responding to those problems.

Why is there a proposed reduction of $15 million? And I guess in the process of answering that I would like you to address what impact a cut of $15 million in our contribution might have for other donors. Are they likely to follow our lead or do we expect that they will make up the difference? What is the position of the Administration here?

Why is this cut proposed? Or is it simply a matter of expecting the Congress to restore the $15 million so you can make the saving in your proposed budget submission?

Ms. BECKER. Thank you, Mr. Chairman, for giving me the opportunity to address these questions.

I would like to point out that the request for fiscal year 1991 is actually an increase of 47 percent over the Administration's request last year of $33 million.

Mr. McHUGH. Well, the Administration's request last year was low. But we have now gone through the process, the budget process for fiscal year 1990, and have reached a number which witnesses tell us is well-received, but still inadequate.

But go ahead, I am sorry.

Ms. BECKER. Thank you.

The other line items in the account that UNICEF is located in also represent very high level foreign policy priorities. These include the UN Development Program, which assists in the economic development and technical assistance programs assisting the poorest of the poor, including children. This account also includes nuclear nonproliferation activities undertaken under the auspices of the International Atomic Energy Agency, a substantial amount for refugees in Afghanistan, again many of whom are children, as well as environmental initiatives.

If you look at the Administration's request this year, the area which receives the greatest increase as compared with last year is UNICEF at 47 percent. The second largest increase went to the aggregated environmental activities and that increase was 33 percent.

This reflects the Administration's concern for the condition of children worldwide, as well as respect for the effective activities of UNICEF, as well as a recognition of the very strong support which the Congress believes UNICEF should get.

Mr. McHugh. Well, I think you have done the best you can do with a bad case. I mean, if you were running UNICEF and received the amount of money from the United States government last year, and then the Administration came in and requested $15 million less than that. What you requested last year is not real to them. That is what the Congress found inadequate.

What is real to them is what they received and what they planned for and what their real needs are in terms of responding. And what they got was $15 million more than you are requesting.

AIDS FUNDING

I would like to make one other point before we have to close, and I am behind already. We talked a bit earlier under Mr. Porter's time about the AIDS funding and the significant role that World Health Organization has played, as well as our own program. But here again, the request of the Administration is for no increase in this program.

Now, my question is what does that request reflect? Does it reflect tight money or does it reflect a sense that we are doing enough in this area? This clearly remains a major threat, particularly in Africa. And is there a problem with the program? Is that what is reflected in this request, or is it simply a matter of tight budget constraints?

Mr. Edelman. It reflects tight money, Mr. Chairman. I do not believe there is any major problem with this program. We all know the horror of AIDS and I think we are making some progress out there.

Between '89 and '90 there was an increase in the budget request for AIDS and essentially, because of the overall budget constraints for foreign aid and within foreign aid, we dropped the request slightly—by $3 million—for '91. In part this also reflects the fact that we have allocated $75 million for a Development Policy Reform Program to support policy reform in development sectors, which could include AIDS.

So it does not reflect a problem that we have with the program.

Mr. McHugh. I am advised—correct me if I am wrong —that there was at least an informal agreement between the Administration and Dr. Mann when he was there that this program would be increased and there would continue to be a 50 percent division of money between our own bilateral program and the World Health Organization's. Is that correct?

Mr. EDELMAN. Dr. Mann did ask me to increase it. I did not respond favorably or negatively to that request, but I do think that the 50-50 split is appropriate at this point.

Mr. McHUGH. That will continue?

Mr. EDELMAN. Well, if the program continues—Mr. Porter pointed out the GPD is under new leadership on the same path as it has before, we have no trouble with the concept of continuing the 50-50 split. However, WHO continues to have problems with implementation in the field, and if these difficulties persist we may want to consider an increase in the bilateral share of this split to compensate.

Mr. McHUGH. Well, thank you all very much. I would like to submit these questions, if I may, and I would appreciate your answering them for the record. I am sorry we do not have more time this afternoon, but we appreciate you being here.

Thank you.

[Questions and answers for the record follow:]

Questions for the Record From Mr. Obey

SUBMITTED TO DEPARTMENT OF STATE

UNICEF

Question. The Administration has requested $50 million for UNICEF for fiscal year 1991. This is a decrease of $15 million over the amount provided in FY-1990. Why has the Administration requested a decrease in funding for UNICEF?

Answer. Our $50 million FY-1991 request for UNICEF in the International Organizations and Programs (IO&P) account is less than the amount Congress appropriated for FY-1990. It is, however, nearly 50 percent higher than our previous year's request. The request reflects the difficult task of balancing the Administration's desire to increase resources for UNICEF while taking account of continuing budget constraints. For this reason the request is still $14 million below last year's appropriation.

Question. A reduced U.S. share for UNICEF has an impact on obtaining funds from other countries. Was this taken into consideration in your request for reduced funding?

Answer. The Administration's FY-1991 request for UNICEF is based on a number of considerations, including competing demands on the budget, and a desire to increase funding for UNICEF. It would be difficult to assess the specific impact of the Administration's funding request on the funding decisions in other countries. Major donors understand and appreciate the need for the U.S. to control spending and reduce the deficit. The United States has always been the largest contributor to UNICEF's core resources, but on occasion other countries (e.g., Sweden) have surpassed the U.S. in extrabudgetary contributions. For other donors, as for us, such decisions take into account a variety of factors, including a country's own economic and budgetary situation.

In making its budget request, the Administration has again emphasized its continued support for UNICEF and the fact that the request, although lower than the level of the previous year's appropriation, has steadily increased each year. The request level is primarily a reflection of our continuing budgetary contraints rather than any diminution of U.S. support for UNICEF and its programs.

Unlike other United Nations organizations, only about 75 percent of UNICEF's financial support comes from governments. The remainder comes from donations by private citizens, non-governmental organizations and groups, and fund-raising activities, such as the sale of UNICEF greeting cards.

Question. UNICEF and the World Health Organization have a goal of immunizing 80 percent of the world's children by the end of 1990. Does the Administration's reduction of funding for UNICEF intend to send a signal that the U.S. no longer supports this goal?

Answer. The U.S. remains a strong supporter of the goal of universal child immunization (UCI) and the UNICEF/WHO goal of immunizing 80 percent of the world's children by the end of 1990.

The Administration's FY-1991 request for UNICEF, although lower than the FY-1990 appropriation, reflects nearly a 50 percent increase over the FY-1990 request and support for UNICEF's immunization and other programs.

In addition to the U.S. contribution to UNICEF's general resources, the Agency for International Development is planning to obligate a million dollars in FY-1990 for immunization and related child survival services which will complement the effort funded from UNICEF's core resources.

As a member of the UNICEF Executive Board, the United States has supported not only sufficient allocation of resources, but also new efforts to ensure the sustainability of immunization programs over the longer-term.

Considerable progress has been made; notwithstanding the level of resources, however, economic conditions in many coutries, as well as war and civil conflicts, continue to act as constraints on efforts to achieve the goal of UCI by the end of 1990.

MIGRATION AND REFUGEE ASSISTANCE

Question. Ambassador Lyman, this morning Roger Winter the director of the U.S. Committee on Refugees testified concerning the shortfall in funding for refugee assistance. Although there have been large increases in the admissions program over the past several years the assistance program has shown little growth. There are more than 14 million refugees in the world and the U.S. share for helping them is decreasing. According to CRS U.S. assistance to refugees has declined from a high of $215 million in FY 1983 to a FY 1990 low of $169 million. The FY 1991 request is slightly below the FY 1983 appropriation and about 25 percent less when inflation is taken into account.

Based on increased funding proposals from both the UN Commissioner on refugees and the International Red Cross how did you arrive at a funding level of $215 million?

Answer. The UN High Commissioner for Refugees is projecting income at the $550 million level for 1990, based largely on the same level of income in 1989. Although his original requests based on needs were at a higher level, the High Commissioner has revised his program budgets to the level of projected income. A U.S. 1990 contribution at the 1989 level of $125 million or 22% is in line with the concept of internationalizing on an equitable basis the UNHCR costs of refugee assistance.

The actions by the International Committee of the Red Cross (ICRC) on behalf of conflict victims are by their very nature unpredictable. It is, therefore, exceedingly difficult to project for purposes of budget requests 18 months in advance of actual needs in ICRC's affected fiscal year. As a result, the administration expects that in the case of ICRC there is great likelihood that the Emergency Fund will have to be used. Indeed, in U.S. FY 1990 we have already had to use the Emergency Fund to support ICRC activities in Panama, Liberia and El Salvador.

The funding level of $215 million for international refugee assistance provides funds designated primarily for the UN High Commissioner for Refugees, the International Committee of the Red Cross, the United Nations Border Relief Operation, and the United Nations Relief and Works Agency. These funds represent a $46.6 million increase over the FY 1990 appropriated level. The amounts included for each organization are based on an estimate of projected requirements in 1991 and of our fair share of those requirements.

Question. What funding deficit will the UN Commissioner on refugees have if the U.S. contribution for FY 1991 is $215 million?

Answer. Were the U.S. to contribute $215 million to UNHCR alone in FY 1991, UNHCR would more than likely have no deficit, since the U.S. contribution would probably represent about 40% of projected budgets.

The $215 million request for assistance is meant to support UNHCR, UNRWA, UNBRO and ICRC in FY 1991. Exact amounts to be contributed to each can only be known when their budgets are in hand. Those budgets will represent the international organizations' best estimates of the needs of their respective beneficiaries, given the emergencies, opportunities, access and events which they project will obtain in 1991. Owing to those many variables and to the uncertainties about levels of support from the other traditional and nay new sources of funding, it is very difficult to predict what UNHCR's funding deficit will be. Trying to respond to the refugee and conflict victim needs resulting from world events in an inexact exercise at the best of times. Given the dynamic character of world events over the past year or two, it would be fool-hardy to venture a guess about 1991. Who would have anticipated the new ethnic violence in Liberia when the FY '90 budget was prepared in the summer of 1988? Or the Nicaraguan election results and the prospects for voluntary repatriation of Nicaraguan refugees from Honduras and Costa Rica?

Question. Last summer there was a reexamination of the refugee admissions program which resulted in a supplemental to meet these needs. Does the Administration have any plans to convene a reexamination of the admissions program?

Answer. The Administration does not have any plans to convene a reexamination of the FY 1990 admissions program. Enactment of the Administration's FY 1990 supplemental request for $70 million, together with currently available funds will cover the requirements resulting from the 27,000 increase in the number of funded admissions as authorized by the President after consulting with the Congress.

Question. One of the major reductions in funding for fiscal year 1990 was in the UNRWA account. The Administration has drawn down $25 million from the emergency fund this year, but an additional $25 million is still available. What is the status of plans to use emergency funds to provide additional assistance for UNRWA?

Answer. We are actively reviewing the option of seeking additional funds for UNRWA from the Emergency Refugee and Migration Assistance Fund (ERMA) to address urgent needs of Palestinian refugees. However, as of this date, the process is not complete. We will advise the concerned committees once a decision has been made.

Question. Last year Congress provided $50 million for the emergency migration fund. This year the Administration has requested only $25 million. Why is there a decrease in funding for this account?

Answer. In requesting a replenishment of $25 million for the Emergency Refugee and Migration Assistance Fund in FY 1991, the Administration recognized the importance of maintaining the ability to respond to urgent and unforeseen requirements as well as the need to stay within the limitations imposed on the Foreign Affairs budget by the Bipartisan Budget Agreement. This request is a significant increase over the Administration's FY 1990 $10 million replenishment request.

REFUGEE ADMISSIONS

Question. On the admissions side more than 400,000 Soviets have applied for admissions to the United States. The ceiling for this year is 50,000. With the unprecedented number of refugees wanting to come to the United States, is there any plan by the Administration to increase the 50,000 ceiling?

Answer. We believe that 50,000 represents the number of Soviet refugees we could reasonably expect to process and admit in FY 1990.

While over 500,000 applications have been distributed, the number received by the Washington Processing Center thus far is approximately 200,000. Some applications represent family groups, others are ony for individuals. Many duplicates are submitted. It is, therefore, difficult to estimate accurately the number of individuals who have actually applied.

The U.S. program carefully concentrates its resources on groups and individuals who are of particular concern to the U.S., including those identified in the Lautenberg amendment (Soviet Jews, Evangelical Christians, Ukrainian Catholics and Orthodox). Therefore, many people who have submitted preliminary questionnaires may never be interviewed.

The final admissions ceiling for FY 1991 will be determined by the President after Executive branch consultations with the Congress later in FY 1990.

Question. If the ceiling is changed will the Administration request a budget amendment to reflect the change?

Answer. If, after consultations with the Congress, the admissions ceiling for the Soviet refugees is set at a number higher than the 40,000 budgeted for in the FY 1991 request, careful consideration would be given to the need for additional funds to cover the increase. When this has happened in the past, the Administration has worked with the Congress to address the imbalance.

Question. In the past there has been a problem with the Administration requesting adequate domestic resettlement costs to follow admissions funding. How has that been coordinated for FY 1990 and for FY 1991?

Answer. As U.S. Coordinator for Refugee Affairs, Ambassador Lafontant takes seriously her responsibilities for the budget as spelled out in the Refugee Act of 1980. As soon as she took office, she involved herself in the preparation of the Administration's FY 1991 budget request and took steps to ensure that the request of the Departments of State and Health and Human Services were mutually consistent.

Ambassador Lafontant chairs a weekly meeting of senior representatives from the Department of State, Health and Human Services and Justice/INS, to ensure policy and program coordination, including budget issues. Furthermore, she closely monitors domestic resettlement programs to ensure that adequate funding is available for high priority programs.

INTERNATIONAL RED CROSS

Question. We often hear of the funding deficit for the UN Commissioner for refugees, but U.S. funding for the International Red Cross has also been decreasing over the years. What is the status of funds we provide to the International Red Cross for assistance and how does it compare to where we were five years ago?

Answer. U.S. contributions to the total budget of the International Committee of the Red Cross (ICRC) have remained relatively constant since 1984 in absolute terms, with the exception of 1985, but have fallen in relative terms as ICRS's total budgetary requirements have risen. Even these levels of U.S. contributions were reached in recent years after extraordinary measures were taken in response to urgent and unforeseen emergencies (and, in some cases, opportunities). Such measures include drawdowns from the President's Emergency Refugee and Migration Assistance Fund (ERMA) and the availability of Dire Emergency Supplemental appropriations with international assistance components. In FY 1990, $2.3 million to date has been drawn down from the ERMA for emergency needs of the ICRC. An additional $200,000 from ERMA has gone to the League of Red Cross and Red Crescent Societies.

U.S. CONTRIBUTIONS TO ICRC
1980 THROUGH 1991

ALL FIGURES IN U.S. DOLLARS

EX. RATE SF S TO $1>>>	2.00	1.96	2.01	2.08	2.32	2.46	1.80	1.46	1.44	1.62	1.60	1.60
ICRC	1980	1981	1982	1983	1984	1985	1986	1987	1988	1989	1990 EST.	1991 REQ.
TOTAL ORDINARY BUDGET EXPENDITURES	18,091,789	21,552,309	24,563,700	24,135,624	29,430,897	31,424,179	48,823,664	60,168,042	71,414,993	59,600,000	$1=SF1.5177 60,950,000	57,810,000
TOTAL U.S. ORDINARY BUDGET CONTRIBUTION	944,347	1,490,753	0	3,813,101	3,983,635	1,882,368	4,612,500	4,738,870	4,375,000	7,200,000	6,095,000	6,000,000
U.S. ORDINARY BUDGET CONTRIBUTION AS % OF TOTAL	5.00%	7.00%	0.00%	16.00%	14.00%	6.00%	9.00%	8.00%	6.00%	12.00%	10.00%	10.00%
TOTAL SPECIAL PROG. EXPENDITURES/BUDGET	53,043,842	50,287,963	60,512,113	54,168,268	78,901,799	123,143,102	103,908,829	101,004,736	132,335,254	177,840,000	225,714,563	215,000,000
U.S. SPECIAL PROG. CONTRIBUTIONS	8,764,049	14,947,979	19,038,233	20,527,153	26,754,023	29,500,397	31,785,722	26,107,259	24,316,704	28,097,000	18,350,000	23,700,000
U.S. SPECIAL PROG. CONTRIBUTIONS AS % OF TOTAL	17.00%	30.00%	31.00%	38.00%	34.00%	24.00%	31.00%	26.00%	18.00%	16.00%	8.00%	11.00%
TOTAL IN-KIND EXPENDITURES	0	0	0	26,699,233	29,446,332	71,335,854	32,585,593	19,656,846	39,886,321	N/A	N/A	N/A
U.S. IN-KIND CONTRIBUTIONS	0	0	0	0	1,421,626	29,630,028	3,784,878	318,097	2,280,656	N/A	N/A	N/A
U.S. IN-KIND CONTRIBUTION AS % OF TOTAL				0.00%	5.00%	42.00%	12.00%	2.00%	6.00%	N/A	N/A	N/A
ICRC GRAND TOTAL	71,135,631	71,840,272	85,075,813	105,003,125	137,779,028	225,903,135	185,318,086	180,829,624	243,636,568	237,440,000	286,664,563	272,810,000
U.S. CONTRIBUTION GRAND TOTAL	9,708,396	16,438,732	19,038,233	24,340,254	32,159,284	61,012,793	40,183,100	31,164,226	30,972,360	35,297,000	24,445,000	29,700,000
U.S. IN-KIND CONTRIBUTION AS % OF GRAND TOTAL	14.00%	23.00%	22.00%	23.00%	23.00%	27.00%	22.00%	17.00%	13.00%	15.00%	9.00%	11.00%

ACTUAL ICRC EXPENDITURES PROVIDED FOR 1980-1989; ICRC APPEALS PROVIDED FOR 1990; AND RP ESTIMATES OF ICRC PROGRAM LEVELS PROVIDED FOR 1991.

Question. Are there plans to increase the U.S. contribution to the Internation Red Cross for FY 1990 and FY 1991?

Answer. Responses to the needs of the International Committee of the Red Cross (ICRC) are considered in the context of all humanitarian requirements. In addition to the Migration and Refugee Assistance Account, steps have already been taken to respond to emergent needs and opportunities addressed by the ICRC. In FY 1990, to date $2.3 million has been drawn down from the Emergency Refugee and Migration Assistance (ERMA) fund for the ICRC. Approximately $25 million remains in ERMA for furture urgent and unforeseen developments. An additional $200,000 from ERMA has gone to the League of Red Cross and Red Crescent Societies. Enactment of a supplemental appropriation for refugee admissions programs will ensure the availability of the ERMA for such assistance requirements

In FY 1991, the request level for the MRA includes a plan to increase assistance levels by some $47 million, some of which will be contributed to the ICRC.

SUBMITTED TO THE AGENCY FOR INTERNATIONAL DEVELOPMEMT

DEVELOPMENT PROGRAMS FOR CHILDREN

Question. Mr. Edelman, the A.I.D. Congressional Presentation for FY 1990 at one point says "one of the social indicators most often correlated with economic growth and development is reduced infant and child mortality." Also, " . . .the persistent problem of malnutrition and famine is a major impediment to human development. Without adequate nutrition, good health is impossible."

But A.I.D.'s funding request does not match these high ideals. Child Survival funding is only increased by $4 million, and there are actual decreases for health (−$9 million), population (−$23 million) and agriculture (−$57 million). Additionally, A.I.D. has the responsibility for preparing the presentations for the International Organizations and, in that, UNICEF receives a $15 million reduction over the last year.

Our public witnesses this morning laid out the great needs in the development areas. Why hasn't A.I.D. followed through on a priority on development programs for children?

Answer. Programs aimed at children remain an integral and high priority component of A.I.D.'s overall foreign assistance program. Direct child survival activities were funded at $203 million in FY 1989 and projections for FY 1991 are approximately $200 million, continuing the relatively high priority A.I.D. accords development funding for children.

Even with current budgetary constraints and competing priorities, A.I.D. places emphasis on development programs aimed at children. However, A.I.D. recognizes that programs benefitting children must be balanced with programs which assist in eliminating underlying poverty, an important contributer to infant and child death and illness.

A.I.D.'s position is that sustainable development programs for children can best be accomplished by creating a policy environment conducive to broad-based economic growth while maintaining assistance for the special and immediate needs of children.

A.I.D. has proposed a new Development Policy Reform Program, funded at $75 million dollars to reinforce developing countries efforts to improve the policy environment for broad-based economic growth and sustainable development. When those resources are allocated, the functional allocations which you cite will be adjusted.

The budget requests for International Organizations are the Administration's requests. The request for UNICEF is the result of an effort to balance requirements for the Administration's bilateral and multilateral development programs, in a climate of severe budget constraints. Althouth the FY 1991 request is $15 million less than appropriated last year, it is nearly 50 percent higher than the FY 1990 request.

Question. Spending for some A.I.D. development accounts is up, for example, the private sector, environment and energy account is up $11 million.

A.I.D. has proposed a $75 million pot of funds for countries making progress on "reforms". Why should children and other individuals in need of development assistance be hostage to the economic and other measures that a government may or may not be interested in implementing?

Answer. Economic reforms are often essential for achieving overall economic stability and for sustained support to improve the economic and social environment for all members of society. Such reforms are necessary for sustaining child survival interventions.

The proposed $75 million dollar Development Policy Reform Program (DPRP), assists countries in implementing essential "development" policy reforms. This $75 million dollars was not taken from any specific account and therefore will have little, if any, effect on funding for A.I.D.'s child-related activities.

Country need, including poverty criteria, is now a part of A.I.D.'s allocation process for assistance to individual countries.

Countries implementing children's programs will continue to be funded regardless of the creation of this separate pot of money. Money allocated specifically for policy reform could improve the policy environment and in turn have a significant impact on the effective implementation of children's programs.

Question. The net effect of reductions in A.I.D.'s bilateral development programs and in UNICEF is a U.S. position to spend less on programs to help children. What effect does this signal have on other donor countries?

Answer. In 1989, A.I.D. obligated over $200 million dollars for child survival programs. The amount of money spent by A.I.D. on child survival-related activities has continued to increase over the past five years.

There are many considerations in the development funding decisions of other donor countries. Small changes in A.I.D.'s budget are not a major influence on other donor governments. Further, by far the largest and most important expenditures on programs for children are the funds allocated by countries from their own resources.

In the conference report accompanying last year's bill, the conferees agreed that funding for all sources for child survival activities for fiscal year 1990 should be targeted at $200 million. Has A.I.D. met that target? What is the Child Survival funding level for all sources in the 1991 request?

Early estimates for FY 1990 indicate that $189 million are planned for activities directly supportive of child survival. We are working with missions and bureaus to ensure that the $200 million level is reached this fiscal year. We do believe that this will happen; our experience over the last four years has consistently shown that the budget numbers for child survival are underestimated at this time of year.

A.I.D. has requested $196 million for child survival activities in FY 1991. This figure reflects the Agency's strong continued commitment to this successful and important program.

DISPLACED CHILDREN

Question. This morning Dr. Neil Boothby described the impact of his work with displaced children in Mozambique. He showed the kind of results that can be obtained in the use of funds for orphans and displaced children. Congress has earmarked funds for these children for the past three years, but the Administration has refused to provide any request for funding in either this year or last year's requests. When is the Administration going to wake up to the value of this program?

Answer. The Administration has responded to the needs of these children. Indeed, services to children across the board constitute a high priority in our development planning. A significant part of our total request for FY 1991, some $200 million in total, goes to meet the needs of children through our child survival efforts. We agree that displaced children constitute a special problem which deserves our attention. Nonetheless, we believe it is preferable to target services to them as part of integrated community development efforts in affected areas. Such efforts can provide a range of health and education services to displaced children, along with specific efforts to reintegrate them with their families and, most importantly, to provide the means for such families to remain intact through improved economic opportunities.

Question. Congress last year also earmarked $5,000,000 for civilians injured as a result of civil strife and warfare. A majority of this funding also goes to help children. Why hasn't the Administration provided an FY 1991 request for this program?

Answer. The goal A.I.D.'s health assistance programs around the world is to increase life expectancy, primarily through decreases in infant and child mortality. Where civil war has created a significant need for curative and rehabilitative assistance, A.I.D. has been and is prepared to help. However, A.I.D.'s program continues to focus on primary health care and disease prevention, rather than curative care and rehabilitation, which are not areas where we have great experience of expertise. A.I.D. has requested funds in FY 1991 to address problems which pose the greatest threat to health in the developing world. These include: immunizable diseases, diarrheal disease, malnutrition, respiratory infection, AIDS, inadequate water supply and sanitation, malaria and other communicable diseases, inadequate or inappropriate financing of health services, and insufficient trained medical and administrative personnel. A.I.D.'s health programs have been developed in consultation with LDC governments and reflect their highest priorites for health assistance. Given the current budget constraints and the need to shape our program to respond to the major causes of death and disability in the developing world, it was not possible to request funds for all health needs in the developing world, including prosthetics assistance.

Question. The Committee in its report last year renewed its request from the previous year that A.I.D. prepare an action plan to address the problems of displaced children. Where is the action plan? Why is it taking so long to prepare?

Answer. We are working on an action plan to lay out the most logical response to the Committee's interest and we expect to have it completed in the near future. However, as discussed with the Subcommittee staff, A.I.D. has found this to be a difficult earmark to administer becaue of the very narrow target group to which it is directed. By its nature, a program to serve orphaned and displaced children is difficult to integrate into Agency programming. Nor does it match the current priorities and capabilities of much of the international private and voluntary organization community with respect to their services to children. In the meantime, we have enlisted the help of our field posts in working directly with their indigenous private and voluntary organizations to identify specific opportunities to assist these children. We are looking into ways to more actively involve the PVO community here in the U.S. in sensitizing their overseas operations to the needs of displaced children.

FUNDING FOR AIDS

Question. The Administration has not requested an increase in the AIDS prevention and control program for FY 1991. However, WHO estimates that AIDS is the single greatest threat to children in Africa. Why is there no increase in funding this year for the AIDS prevention program? Any why do you feel that the program should not be expanded?

Answer. HIV infection, and consequently AIDS cases, are continuing to increase worldwide. In some areas, the increase is alarmingly rapid. In parts of Africa, the Caribbean, and Thailand in the Far East, infection rates have reached between 10 and 30 percent of higher among some high-risk populations.

While these trends are unlikely to be reversed in the short term, there are some signs of progress. Follow-up operations research on some of the programs shows that people's knowledge of the disease is improving. Reports also indicate that people are beginning to change their high-risk behavior as a result of this newly acquired knowledge.

Despite the recent progress, it is clear that no single donor can meet all the needs in the AIDS area with the funds that are available or being requested. Additionally, A.I.D. has to operate within funding constraints given the overall fiscal situation and competing program priorities. There are a number of other areas in A.I.D.'s program where the situation is as serious and the needs are as urgent. The difficulty lies in balancing these choices.

Given those contraints, A.I.D. believes that the FY 1991 funding request is a reasonable one and will enable the Agency to continue to make progress in addressing the AIDS situation.

Question. Last year funding for AIDS was split between the A.I.D. bilateral program and a contribution to WHO. What is your projection for the funding distribution for FY 1991?

Answer. The World Health Organization's Global Programme on AIDS (WHO/GPA) remains intact despite the resignation of its director, Dr. Jonathan Mann. Except for designating Dr. Michael Merson as the acting director of GPA, no changes have been made in the program or the staff. Consequently, A.I.D. continues to support the WHO/GPA.

Yet, the ever-present problems of implementation still persist. Particularly in Africa, WHO continues to have difficulty moving funds and getting new programs started.

At the present time, the Agency continues to support a 50/50 division of its resources between GPA and A.I.D.'s bilateral activities. However, if GPA continues to have problems implementing field programs, A.I.D. would want to consider increasing its bilateral programs to compensate. Consequently, to assure adequate programming flexibility, the Agency would prefer that no legislative earmark for WHO/GPA be placed on the FY 1991 budget.

Questions for the Record From Mr. McHugh

SUBMITTED TO DEPARTMENT OF STATE

FAMINE IN ETHIOPIA AND SUDAN

Question. Mr. McHugh. Briefly, what is the U.S. doing to prevent mass starvation in Ethiopia and Sudan? Are large numbers of Eritreans going to starve in spite of our current efforts? How many of these do you estimate to be children?

Answer. The U.S. Government has provided $127 million to date towards emergency famine relief in Ethiopia in 1989-1990. That includes funding for 233,200 MT of emergency food for the north, of which approximately 74,000 MT has been delivered so far. The U.S. has also provided 5 water tanker trucks, six food transport trucks, 30,000 blankets and 375 rolls of plastic sheeting. Grants have been made to support relief efforts through the Catholic Relief Services and the U.S. AID mission.

Refugees in Ethiopia from Sudan and Somalia are not in danger of starving at present but are almost wholly dependent on food brought in by the donor community. The U.S. provides about 25% of UNHCR's Ethiopia budget which will reach over $45 million this year. We also provide a major share of the food commodities through the World Food Program.

U.S. relief to Sudan's conflict victims increased dramatically in 1989 under Operation Lifeline Sudan I (OLS I). In 1990, assistance continued under the aegis of OLS II and through the ICRC. U.S. relief has concentrated on providing seeds and tools, drilling wells, inoculations, emergency food relief, plastic sheeting and blankets, and administrative and logistical support for the relief effort. The total U.S. Government contribution for 1989 and 1990 to date is $91 million.

Approximately 2.1 million people are estimated to be at risk in Eritrea, but recent reports indicate that conditions in Eritrea may not be as critical as we feared in October 1989. Food is reaching people from Sudan and on-farm stocks may be better than we thought. However, the threat of massive famine in Tigray, with an estimated at-risk population of 1.4 million, remains.

We do not know how many of those at risk are children. However, large numbers of children, who are particularly vulnerable, can be expected to die if adequate foo relief cannot be provided.

Question. What percentage of U.S. relief food is actually getting through to those who need it in both Ethiopia and Sudan, and is not lost, stolen, or damaged?

Answer. During and after the Eritrean People's Liberation Front attack on the port of Massawa, almost 50,000 MT of relief food was lost. Some of that food was U.S. relief grain. Other than that, we believe that no U.S. food has been lost, damaged, or otherwise diverted from the famine relief effort in Ethiopia. Part of the reason for our insistence on full access to refugees in Ethiopia is to ensure, on a routine basis, that food aid is being used correctly.

There were some losses of U.S. provided food commodities in Sudan in 1987 and 1988. For the years 1989 and 1990, we believe, for the most part, that U.S. food relief is reaching its intended beneficiaries.

Question. Who is taking the lead in the relief efforts and is that leadership effective? Are we working closely with the Soviet Union in Ethiopia?

Answer. The United States Government has been a key player in organizing famine relief efforts in both Ethiopia and Sudan, but in both countries we believe the United Nations should play its customary role as the coordinator of donor relief efforts and as the chief spokesman for the donor community. In both Ethiopia and Sudan, where Mr. Timothy Painter and Mr. Michael Priestley respectively are the Secretary General's Special Representatives, the U.N.'s efforts are well led. Refugee relief is also handled multilaterally with UNHCR in the lead. UNHCR staffing is of mixed quality as with any large organization. We have had concerns about the leadership of the country representatives in both Ethiopia and Sudan.

In Ethiopia, we have worked with the Soviet Union in our efforts to move relief efforts forward, and they have been helpful.

Question. To what extent are the Government of Ethiopia and Sudan cooperating in the relief effort with international donors? What steps has the Administration had to take to encourage their corporation?

Answer. With respect to famine in Ethiopia, the Mengistu regime has been helpful on some matters, but obstructionist in others. The southern route, which runs north from government-controlled areas in central Ethiopia to rebel-held Wollo and Tigray provinces, could not have opened without permission from the highest levels of the Ethiopian government. At the same time, the government in Addis Ababa has refused repeated calls to allow relief flights into Mekele, (in rebel-held Tigray) or to allow relief food to move through the northern port of Massawa, (which is now held by the Eritrea People's Liberation Front) into famine stricken Eritrea and northern Tigray.

With respect to relief for refugees from Sudan and Somalia, the Government of Ethiopia's record is also mixed. It has accorded asylum to the refugees (some Horn countries have not), but it has not provided UNHCR with completely free access to refugee camps nor has it provided fully for law and order to protect refugees.

We have spoken with the Government of Ethiopia on several occasions to stress the importance of the several relief efforts and to urge its cooperation. We pushed very hard to get the southern corridor open, and we continue to press the Government of Ethiopia to allow relief flights to Mekele, to reopen Massawa, to stop bombing relief convoys, and to ensure the strictly civilian character of refugee camps. We are working closely with other donor governments, including the Soviet Union, to ensure the international community is speaking with one voice in this effort.

The Government of Sudan has also been uneven in its support of relief efforts. It has been diplomatically very supportive of relief efforts in northern Ethiopia that would mitigate any further refugee influxes to Sudan. Regarding relief efforts for southern Sudanese conflict victims, on March 26, the Government, the U.N. and the donors signed an agreement to allow a Phase II of Operation Lifeline Sudan. This was a significant first step in getting relief efforts underway again. In the weeks since the Government of Sudan signed the agreement there have been continuing problems in implementing this large, complex relief effort. But some relief operations are underway, and we will continue to work closely with the U.N., the ICRC, other donors, PVOs and the Government of Sudan.

Question. What can be done to break the cycle of famine in the Horn of Africa? How long should the American people be expected to continue the large-scale feeding of millions of Africans?

Answer. The American people have been and continue to be very generous with respect to relief efforts for Africans affected by drought and conflict, reflecting the great American humanitarian tradition.

In the last decade the problem of famine in the Horn of Africa has not been caused simply by drought or inadequate agricultural development programs or policies. Political instability, such as the ongoing civil wars in Ethiopia and Sudan, continues to be the major factor in famine situations. The cycle of famine will be broken only when political solutions are found to these conflicts.

REFUGEES

Question. Why is the U.S. share of support for UNHCR and average support per refugee declining?

Answer. The dollar level of the U.S. contribution to the UNHCR has not varied greatly over the past decade, but the doubling of the number of refugees worldwide and the resulting program increases of UNHCR have caused the percentage U.S. contribution to UNHCR to decrease steadily during the 1980's. That percentage hit a high point in 1982 of 30%, and decreased gradually to 21%, but has held steady at that point for 1988, 1989, and what we project for 1990 (assuming no new program increases).

Per capita refugee expenditures on the part of the international community as provided through international refugee organizations have slipped since 1985. U.S. contributions to international refugee organizations have also declined when calculated on a per capita basis, from approximately $25 per refugee in 1985, to about $16.50 per refugee in 1989.

The decline in the U.S. percentage share is best understood by looking at the large increases in the numbers of refugees in the past several years and at the corresponding increases in program levels of UNHCR associated with both increasing needs and opportunities. The largest increases in one year's refugee population since 1985 occurred from 1987 to 1988 and then again the following year. In that 24 month period, 2.3 million new refugees appeared, worldwide.

The program levels of UNHCR increased by 20% from 1987 to 1988. Funds available for U.S. refugee assistance simply have not increased at the same rate as the number of refugees worldwide or the program levels of UNHCR, ICRC, UNBRO, UNRWA, the major organizations to which we contribute.

In addition to the increase in the number of refugees worldwide and international refugee organization program increases, there have been other pressures on the Migration and Refugee Assistance account on the admissions side. In the past 2–3 years, extraordinary admissions opportunities have become possible for political prisoners in Cuba; Amerasian children, reeducation center detainees and others from Vietnam; and for persecuted religious minorities in the Soviet Union. Ideally, of course, there should not be any either-or competition between refugee assistance and refugee admissions funding. We acknowledge the reality, however, that there is inherent competition among all federal programs as part of our national deficit-fighting strategy.

A further drain on refugee assistance resources provided under the Migration and Refugee Assistance account stems from Congressional earmarking of particular programs outside the funding level requested by the Administration. Because no additional funds have been provided for these earmarked programs, the only option has been to reduce funding available for other refugee programs. Earmarking has had a significant negative impact on U.S. contributions provided to the international refugee organizations for each of fiscal years 1988, 1989, and 1990.

Question. Is the ERMA account being used to give the impression that the current services level is essentially unchanged from FY 1989 to FY 1990? If so, isn't this contrary to the purpose for which ERMA was established?

Answer. The Emergency Refugee and Migration Assistance (ERMA) Appropriation, as defined by the Migration and Refugee Assistance Act of 1962 (MRAA), as amended, is available only for "unexpected urgent refugee and migration needs," and only after a Presidential determination that the provision of assistance in response to such needs is "important to the national interest."

In 1979, the GAO ruled that the "unexpected urgent" language in the Act limits use of the emergency fund to needs that (1) "were not foreseen and not planned for in the regular budget process . . . [including] . . . needs which the Administration cannot reasonably have been expected to anticipate," and (2) "must be satisfied immediately and cannot await the enactment of supplemental and appropriation acts."

Use of the ERMA has been and will continue to be consistent with the MRAA and the 1979 GAO ruling.

Question. The Congress has always intended that refugee aid be provided in a way that treats all refugees equitably. Can you say that your program does that?

Answer. It is not possible to provide each refugee in the world with precisely the same level of assistance. Some of the factors affecting what can be accomplished include host country infrastructure and the standard of living of surrounding local communities. In their programming of assistance to refugees, however, the international organizations which we support are equitable, applying established standards in each of the sectors (health/nutrition, food, water, shelter, etc.)

The third of the three lasting solutions to refugee situations is third country resettlement, the preferred solutions being voluntary repatriation and local integration in the country of first asylum. Third country resettlement (admissions in U.S. refugee parlance) is by definition more expensive than the other solutions. In that sense, then, it can be said that the refugee program is inequitable. It is an inequity, however, that the congress and administration tolerate in an effort to provide the solution of third country resettlement to refugees in whom the U.S. has an interest, while continuing to assist the vast majority of refugees in countries of first asylum. This manner of doing refugee business is endorsed by the international community; other countries similarly provide resettlement opportunities to relatively small number of refugees.

SUBMITTED TO THE AGENCY FOR INTERNATIONAL DEVELOPMENT

CHILD SURVIVAL IN SUB-SAHARAN AFRICA

Question. A.I.D.'s Congressional Presentation for Africa states on p. 27 that just in the next decade alone 270 million children will be born in sub-Saharan Africa, more than the current population of the United States. Are we ready for these children? Do you think your request level for Africa of $560 million for the entire continent (about $1 per person for over 40 countries and for all A.I.D. activities) is sufficient to set the basis for addressing the needs of this generation of children?

Answer. Severe constraints on foreign assistance and the competing great needs in other parts of the world restrict the overall magnitude of the Administration's request for the Development Fund for Africa (DFA) for FY 1991. Thus, it is especially critical that we focus our resources to contribute as effectively as possible to the process of bringing about sustainable economic growth so that countries can meet their people's needs. Likewise, for the people of sub-Saharan Africa, real social and economic progress is going to require not only a continued flow of external resources but, perhaps more importantly, a significantly more efficient use of their own resources.

Our effort to use A.I.D. resources as efficiently as possible has been somewhat hindered by the need to respond to too many special interests, which while important, are peripheral to the process of bringing about sustainable economic growth. Congressional assistance in keeping these additional requirements to a minimum would be especially helpful to us in meeting our objectives under the DFA.

For the foreseeable future, A.I.D. will be a relatively small donor in sub-Saharan Africa, with other donors providing 15–20 times as much assistance as we do. Although resources fall far short of what is needed, what we can do is to leverage our resources to bring about greater sustainability, more efficiency, and better services.

Question. At current infant and child mortality rates, how many of these children will likely die in infancy? By the age of 5?

Answer. At the current rates of infant (0–1 year) and child (0–5 years) mortality, estimated to be 110 and 181 per 1,000 live births, respectively, approximately 30 million out of 270 million infants born during the 1990's will die during the first year of their lives. About 50 million children will not survive to their fifth birthday.

There has been significant improvement in infant and child mortality rates over the past 20 years and particularly over the past ten years. To illustrate this, if the infant and child mortality rates of ten years ago had remained constant, 5 million more infants would have died in their first year and 8 million more children would not have survived to age five.

The current levels of infant and child mortality in sub-Saharan Africa are still high. A.I.D. will continue its efforts, including through the Africa Bureau's child survival and family planning projects, to reduce these rates. According to a UN estimate, by the end of this decade the infant mortality rate will decline to 90 per 1000 births and to 250 per 1000 births for children under five. Based on present trends and planned interventions, we believe this can be accomplished in the great majority of countires in the region.

Question. What are the implications of such a large population increase for primary education? For food production? For the environment? And, ultimately, for secondary education and gainful employment? Given these implications, do you still think the request for sub-Saharan Africa is adequate?

Answer. The increasing population of sub-Saharan Africa represents an enormous development challenge, particularly in our efforts to make the most effective use possible of limited resources. Meeting this challenge will require higher returns on investment and broader tapping of the energy and productivity of the African people. This is why, in implementing the DFA, we are focusing our resources to contribute as effectively as we can to the process of bringing about sustainable, broad-based, market-oriented economic growth so that countries can meet their people's needs for food, housing, education of jobs; increasing productivity through the improvement of job related skills; and improving food security for countries and individuals who do not produce enough to meet their own consumption needs.

The Administration's request for assistance to sub-Saharan Africa is not and could not be adequate to meet all these needs. It is what the United States can afford, considering critical domestic and international requirements.

Question: On p. 34 of the Africa Annex, A.I.D. states that there is no direct relationship between infant mortality rates and traditional forms of interventions such as oral rehydration therapy (ORT) and immunization. Please explain what the primary causes of infant and child mortality are in sub-Saharan Africa and what A.I.D. is doing to address them.

Answer. Recent data confirm that many factors contribute to infant mortality, including diarrhea, for which oral rehydration therapy (ORT) is an effective and practical intervention, and diseases which affordable vaccines can prevent. These data show that while ORT and immunization are highly effective interventions in some settings, they are not sufficient to reduce mortality dramatically in others, such as Malawi, where infant mortality rates are complicated by acute respiratory disease and drug resistant malaria. Currently, we estimate that malaria accounts for about 30 percent of all deaths among African children under five years of age.

For more than a decade, A.I.D. has supported a major survey, the Demographic and Health Survey, being carried out in many developing countries all over the world. The findings indicate that many factors contribute to infant and child mortality. Immunizable diseases, diarrheal disease, acute respiratory disease, malaria, and malnutrition are among the many factors that cause infant mortality. With known and effective treatments for immunizable and diarrheal diseases, A.I.D. has decided to funnel its limited resources toward attacking these major killers. A.I.D. is addressing the other causes of mortality by exploring ways in which these health problems can be dealt with most effectively. So far, demographic and health surveys have been conducted in 14 sub-Saharan African countries, but the data have become available only recently.

In close collaboration with the National Academy of Science, A.I.D. has established a panel of eminent scientists from several disciplines to examine in detail the various factors possibly affecting child survival, including specific primary health care interventions. We are confident that the panel's report, which we expect to be issued early in 1991, will shed increasing light not only on the primary causes of infant and child mortality in sub-Saharan Africa but also provide practical guidance for future A.I.D. action in this regard. But, as with most of the serious problems of the developing world, solutions are rarely as simple or direct as we would like.

Question. To what extent are you using family planning to promote child survival through child spacing?

Answer. Child spacing is becoming a key component of our child survival strategy and programs in sub-Saharan Africa. In recent years, African governments have come to accept child spacing as an accepted health intervention based on its public health value for protecting the lives of high-risk mothers and infants. Some 34 countries now have family planning policies in place.

Overall in Africa, about 40 percent of A.I.D. funding in public health goes to programs for family planning and child spacing. In future years, we expect to increase the emphasis on child spacing.

STRUCTURAL ADJUSTMENT AND THE VULNERABLE

Question. During the 1980's, over thirty African countries adopted economic stabilization and structural adjustment programs, usually with IMF-World Bank support. Yet not only did predicted growth not occur for the most part, it was the lowest income and most vulnerable groups, including children, the aged, women, the disabled, etc., that bore the brunt of the impact of these reforms. They faced higher prices for staples, increased unemployment, budgetary reductions for health and education, etc. In response, people have rioted in such places as Ghana and Zambia. Does A.I.D.'s pursuit of sustainable, broad-based and market-oriented economic growth satisfactorily take into account the impact of structural reforms on the most vulnerable groups?

Answer. We have studied and will continue to study closely the question of the effect of structural adjustment on vulnerable groups. Based on analyses to date, we believe that there is no evidence that these programs systematically harm vulnerable groups.

Our research suggests the following generalizations are supportable: (1) reform programs have led to a reduction in marketing costs, which has meant a *fall* in real food prices in the majority of African countries for which we have data, even though producers have received higher prices; (2) reform programs have been followed by a contraction in health and education expenditures in half the countries for which we have data, and by an *expansion* in expenditures for health and education in the other half; and (3) most of the vulnerable earn their livings in the informal economy and are not directly hurt by contraction of formal sector employment. Nevertheless, we are mindful that poverty is rife in Africa, and adjustment programs must, to the extent possible, be concerned with poverty alleviation. Our programs, therefore, include some or all of the following characteristics:

(1) concentration on increasing equity and efficiency in the health and education systems—shifting resources from curative health care to primary health care and from tertiary education to primary education;

(2) focusing on ensuring that market liberalization leads to competitive solutions, and not oligopolistic ones, so that consumers and producers also benefit rather than just traders and middlemen;

(3) eliminating legal and regulatory restrictions on the operations of small, informal businesses;

(4) examining land tenure laws, rules determining access to common property (such as forests), rules determining access to credit, etc. to see if changes are needed to increase equity; and

(5) establishing a process of discussion and consultation between government and groups affected by any policy change, in order to make the changes more acceptable and more sustainable.

THURSDAY, MARCH 29, 1990.

MISUSE OF FOREIGN AID FUNDS

WITNESSES

SHERMAN M. FUNK, INSPECTOR GENERAL, DEPARTMENT OF STATE

GEN. HERBERT L. BECKINGTON, INSPECTOR GENERAL, AGENCY FOR INTERNATIONAL DEVELOPMENT

FRANK C. CONAHAN, ASSISTANT COMPTROLLER GENERAL, NATIONAL SECURITY AND INTERNATIONAL AFFAIRS DIVISION, GENERAL ACCOUNTING OFFICE

STEPHEN A. TRODDEN, ASSISTANT INSPECTOR GENERAL FOR AUDITING, DEPARTMENT OF DEFENSE

CHAIRMAN'S OPENING STATEMENT

Mr. MRAZEK. I will call the meeting to order.

This morning we are going to hear testimony concerning the misuse of foreign aid funds. I'm not sure that is the best title for a hearing like this. But it is the first time that the subcommittee has dedicated an entire hearing to this topic, rather than simply covering individual problems on a case-by-case basis during our regular hearings.

We are hoping that this kind of direct approach will bring a greater emphasis to the topic and greater attention from the administering agencies who are responsible for correcting these problems.

Certainly, the topic is a lot more expansive than just sexy corruption cases, the kinds of things that we see all too frequently in the newspapers—theft, bribery, kickbacks and various crimes by other governments and government officials.

The topic also includes, and perhaps more importantly includes, the efficiency and effectiveness of our foreign aid programs in achieving results. Issues of poor management, lack of control, lack of accountability are often far more important than many of the corruption cases which are interesting to hear about but which involve relatively few dollars, compared to those programs where we are spending huge amounts of Federal money and not achieving positive results.

Today, we will be hearing form Herbert L. Beckington, the Inspector General, Agency for International Development; Mr. Sherman M. Funk, the Inspector General at the Department of State; Frank C. Conahan, the Assistant Comptroller General from the General Accounting Office; and Mr. Stephen Trodden, the Assistant Inspector General for Auditing in the Department of Defense.

I will ask Sherman Funk, the Inspector General, to begin first. Mr. Funk.

MR. FUNK'S OPENING STATEMENT

Mr. FUNK. Thank you, Mr. Chairman.

With permission, sir, I would like to enter my statement for the record and just give a very boiled down version of it orally.

Since this is the first time I have addressed this particular committee, the committee staff asked me to give a rundown, very briefly, of my organization, which is a bit different from some of the other IGs.

I have, as do all of the IGs, Offices of Investigation and Offices of Audit. In addition, I am required by the Foreign Service Act, which is incorporated into my legislation, to maintain an Office of Inspections. You will see why this is important in a moment for this particular hearing.

We review every year between 80 and 90 posts worldwide, plus four to six bureaus in Washington. That is done by my inspection corps.

Last January, January of 1989, at the request initially of Secretary Shultz and then confirmed by Secretary Baker, I set up an Office of Security Oversight. One of the things we are looking at in that office is our Antiterrorism Program.

I would like now to go to the substantive areas for the hearing. Let me start with security.

SECURITY

The Security Oversight Program I have is headed by Terry Shea, who is the Assistant Inspector General for Security Oversight. He was Director of Security at NATO for nine years. I put together a staff under Mr. Shea of experts in various phases of security. We do basically three things.

We start from ground zero by looking at the threat, the definition of the threat—critical, high, medium or low. Then we determine whether or not this threat was realistically developed, was it accurately developed. I am talking on a post-specific basis because, until now, all of our security standards, in effect, have been global. If they relate to a high threat post, then it becomes a high threat worldwide, and we know the same threat reaction also applies worldwide. That seems not to be a very sensible way of doing it.

Then we look at the security standards developed here in Washington to counter these threats. We look at how those standards are promulgated, issued across the world. Then, finally, we look at how the various posts and consulates react and counter the threat.

That, basically, is the mission of my Office of Security Oversight. I have both inspectors and auditors in that office.

My inspectors represent a very broad range of technical talent in the area of security and intelligence. My auditors basically were moved over from my Security and Intelligence Division in my Office of Audits.

So, let me comment first on the security issue and the reviews by my security oversight people.

The difficulty has been, until now, that our standards have been set in reaction to the Inman Report which, in turn, reflected the terrorist bombings in Beirut and elsewhere. Initially, as a result of that, we have set standards worldwide that require things like 100 foot setbacks, a whole range of special equipment, ballistic glass, etc. They require access controls which make it almost impossible to get through, except by using heavy artillery.

We have done that worldwide. But the point I would like to make, Mr. Chairman, is that there is an inherent risk in serving overseas. Our people in the department recognize and accept that risk. Otherwise they would not be Foreign Service Officers.

Now, the other side of the coin is that they are also worried in many posts about crime, because their families are at home when they are at work and the crime factor tends to be increasingly important in the eyes of many in the department.

We only have a few posts that are a critical threat with crime. We just returned from one in Brazil, where Rio is in that category.

When we get to the post, we look at these things. We look at physical intrusion, including terrorism—either mob, as we had in Islamabad some years ago, or almost in the case of Tegucigalpa. We look at the technical intelligence threat: are our facilities vulnerable to flooding? Can people tap into our communications? We look at the humint threat. Finally, we look at crime.

We do these in all of our inspections, and we have experts in each of these categories.

The difficulty is that the Department does not have money, it doesn't have the resources to meet the need. If we are going to have all of our posts so hardened, so impervious to attack, the cost to the taxpayers would be astronomical. So we settle for something less than that.

However, that something less has, for all intents and purposes, represented perhaps the best reaction, and that is against terrorism.

Since the program has been in effect, there has not been any significant, certainly no successful, attack on any of our posts.

We now are inspecting the Bureau of Diplomatic Security. This is the largest inspection that I have mounted since I have been there in two-and-a-half years.

In diplomatic security, you have almost 1,700 people. It's the largest bureau we have. The Anti-Terrorism Assistance Program, the ATA Program is located in that bureau. We are taking a particularly hard look at that as part of our inspection.

What may come out—and it is too early to tell—is that at the conclusion of our inspection, which is underway right now, we may decide that it is advisable for us to do a further look separately at anti-terrorism, to find out if, in fact, the various elements of that program are working. Are the funds in the anti-terrorism area being well spent? Are we getting the bang for our buck that we should in terms of the quality of training, the police training overseas, that ATA funds are paying for?

This will require an in-depth audit. It is entirely likely that, as a result of our inspection, we will go on and do such an audit.

But I do think I should stress that the anti-terrorism aspects of our security programs have been clearly the most successful. We have put up embassies which are military fortresses in some cases.

My problem is we have been doing that on a uniform basis, and, sometimes, the real threat has not been physical intrusion or mob intrusion. The real threat has been technical. Ironically, it is much less expensive to counter a technical threat than it is a physical threat.

The fact of the matter is that one of our basic conclusions, so far, after a little over one year of this program, are that we do not yet have enough posts around the world in which we can store, process, work, and talk in a secure manner. This is one of the major security weaknesses we flagged which is being addressed now by the department.

We also found too often that some posts are not equipped to deal with emergencies. The emergency action plans, which are required in all security work, are not there in place. If they are in place, they tend not to be sufficiently flexible.

REFUGEE ASSISTANCE PROGRAMS

In the refugee assistance area, we have scheduled an inspection of the Bureau of Refugee Programs starting next month, early next month. We do not, as yet, have any completed report in the refugee area.

The audit we are going to begin is focusing on the Refugee Admissions Program in Southeast Asia. I have also assigned one of the CPA firms we have under contract to assess the adequacy of financial accountability of various, selected, cooperative agreements that we have negotiated between the Bureau of Refugee Programs and joint voluntary agencies.

However, our regular inspection program has highlighted a number of difficulties, which we will be looking at in more detail in our audit. For example, in Bangkok, we found that the joint voluntary agencies tend to equate the ceiling on admissions we fund with a goal. Inevitably, whatever ceiling we set for funding becomes the goal of the voluntary agency.

Whether or not that is a realistic figure, they try to shoot for it.

The second aspect of this is that the embassies tend to feel, too often, that the voluntary agencies are processing people without regard to the distinction between their being political refugees and economic refugees. In other words, a great many are leaving for economic reasons—flooding into our camps, flooding into the system for handling them.

This is something that requires substantial attention.

INTERNATIONAL NARCOTICS CONTROL

The area under the aegis of your subcommittee, sir, to which we have given the most attention, is narcotics control. Thus far, we have had teams review the status of our anti-narcotics work in Peru, in Bolivia, in Thailand, in Pakistan, and in Burma. We have completed a major inspection of the Bureau of International Narcotics Matters. We have completed field work in Mexico as well.

We have issued a number of reports on this. The Southeast Asia audit report is classified, however, and it would be difficult for me to discuss too much of it in an open hearing. But much of the others I can cover.

There is no doubt that we have had severe problems in the area of countering drug trafficking. In a nutshell, one conclusion we arrived at, looking at Peru, is that coca eradication has not really succeeded. It is not being done at all now, of course, in Peru, and in Bolivia it is continuing. The overwhelming response is that there is more coca being produced now than ever before.

We have also done some work in the aviation spare parts area. The State Department is now a major operator of aircraft. We have about 150 aircraft, almost 200, rather, worldwide. We own 50, roughly, outright; another 150 we transferred ownership on, but we support them.

We have some serious problems with the aircraft spare parts program. Just recently, several weeks ago in Florida, at the Opa Locka installation where we house our aircraft and maintain them, we have arrested five persons for selling State Department spares and making a handsome profit on the deal illegally.

When I testified last July before a Senate Subcommittee, I especially commended the dedication, the courage, and the professionalism of the people who are involved overseas—our INM people, DEA, Defense, and other agencies.

I noted with some understatement that they are carrying out a difficult and very dangerous effort. I said that I think we owe it to them to help make sure that the support they need is not blocked or hindered back in Washington by inadequate coordination or by bureaucratic inertia and nitpicking.

Some of the gravest difficulties in this whole area have arisen because of various turf fights in Washington. Fortunately, those kind of turf fights very rarely materialize in the field. The trouble is back in Washington.

I should caution that much of our information goes back to audits and inspections that were conducted six to 12 months ago. There is a new team in the department now, including a new Assistant Secretary for International Narcotics Matters. The bureau has accepted most of our recommendations and they say they are implementing them.

I have no reason to believe they are not, but I cannot verify that, of course, until we do follow-on work.

But I must also say that the difficulties are very real. Let me just tick off some of the things that we have recommended.

We think it is important that the State Department develops a plan for AID and State Department cooperation. We have had a few successes in this area, and they tend to relate the use of alternative crops.

In one case, for example, in Makaland, in the northwest part of Pakistan there was an excellent program which sharply reduced poppy production. If the follow-on work could have been picked up by AID, we would have a situation where crops, where the opium crop, the poppy crop, has actually been almost wiped out.

The difficulty, sir, again here is that there is not enough close coordination between AID and the State Department.

These things do not happen in a vacuum. There has to be an initial, up-front effort by us, in the State Department, and in AID to pick up the follow-on work. Otherwise, inevitably, as soon as our funding stops for a specific area, for a specific project, they'll go back to the high profit crop, and we will be back to the status quo.

We think there must be alternative strategies for crop eradication. In Pakistan, for example, we sent a turbo-thrush aircraft over, and at some considerable cost, too. We flew it over from the States. It did all of two days worth of eradication, and that is all. It had two days of use.

We think that we have to think this whole thing through, that we should plan better, that we should allow for the local resources, instead of trying to transport everything ourselves from the States.

We believe we have to have our embassies do a more effective job of monitoring the end-use of the equipment that we send them. There are too many cases where graft and corruption have mitigated against effective use of the equipment that we send over at some substantial cost.

We have to look at the efforts of our NAUs, the Narcotics Assistance Units, to go out in the field, to get away from the embassy, to go out in the field and see how things are happening there, and to ride closer herd on the sub-units that are established in the field.

Our conclusion so far has been grim. The fact is there are few signs of success. What signs there are show there have been many, many hectares of coca eradicated in Peru and Bolivia, and some in Ecuador. There have been many hectares of poppy seed eradicated. But the net result is that the drugs are flowing in at a greater level than ever.

So our conclusion is that we are either going to have to do more of what I am talking about or else rethink the basic strategy.

I would be happy to answer any questions.

[The prepared statement of Mr. Funk follows:]

STATEMENT OF
SHERMAN M. FUNK, INSPECTOR GENERAL
U.S. DEPARTMENT OF STATE
BEFORE THE
SUBCOMMITTEE ON FOREIGN OPERATIONS, EXPORT FINANCING AND RELATED PROGRAMS
HOUSE COMMITTEE ON APPROPRIATIONS
ON
MARCH 29, 1990

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Mr. Chairman and Members of the Subcommittee:

I am pleased to have this opportunity to appear before you today to discuss the work of my office in general and to focus on several areas of particular interest to the committee: antiterrorism, international narcotics control, and refugee assistance.

While the Department of State has a long tradition of an Office of Inspector General for the Foreign Service, the new Office of Inspector General for the Department of State was established in 1986. I was sworn in as the first independent Inspector General (IG) of State in August 1987. We have now attained nearly full staffing, with personnel in place or selected for 92 percent of our 262 authorized positions. In addition to the audit and investigative functions required by the Inspector General Act, the Foreign Service Act of 1980 requires that we inspect each post abroad at least once every five years. I therefore also have a mandated inspection function.

Pursuant to the Omnibus Diplomatic Security and Antiterrorism Act of 1986 (P.L. 99-399), the Secretary of State bears primary responsibility for the physical and technical security of personnel and facilities at our 258 posts overseas. In December 1988, then-Secretary Shultz requested me to establish a new function to provide appropriate inter-agency oversight of the Department's security programs. Secretary Baker reaffirmed this request, and my Office of Security Oversight (OSO) became operational in January 1989. The establishment of OSO resulted in an increase of 23 positions, reflected above, to meet the inspection and audit demands of this new responsibility. Most of these positions have now been filled by highly qualified security experts drawn both from the Department's Bureau of Diplomatic Security and other government agencies. The OSO staff was further augmented with auditors transferred from the Office of Audits' former Security and Intelligence Division.

Although the law requires post and bureau inspections on a five-year cycle, we conduct them, in fact, every three years. This shorter cycle coincides with the average term of an Ambassador at post so that each post is inspected at least once during an Ambassador's assignment. This means that we inspect approximately 90 posts and four to six bureaus each year. In FY 1991, our inspections will continue to focus on senior and mid-level managers' performance as a means of increasing management's accountability and integrity. Inspection teams concentrate on the conduct of foreign policy; the quality of post management; the adequacy of internal controls; inter-agency coordination; and the prevention of waste, fraud, abuse and mismanagement.

Our inspection function also includes compliance follow-up review teams which visit posts six to twelve months after an inspection to check whether the posts actually did what they told us they were going to do. This compliance follow-up review puts teeth into our recommendations. Once we identify a problem, we don't just go away. The Department must take action upon our recommendations or explain why not and what alternative actions will be taken.

During FY 1989, inspectors completed 51 reports which assessed operations at 82 posts abroad. Eighteen additional inspections are in process or nearing completion. Compliance follow-up reviews have been performed at 17 missions to verify compliance with previous inspection report recommendations. Four posts were commended for outstanding leadership and management.

In addition to our current areas of review, other programs and activities will be selected for audits and inspections according to their significance to the promotion of major Departmental goals, their magnitude in dollars and other resources, and those areas of particular interest to the Congress and the President, the Secretary, and other Department principals.

The Office of Security Oversight will continue its inspection of security at our posts overseas, the management of the Bureau of Diplomatic Security, the computer security programs, and the application of construction security standards. OSO will also continue to audit high cost and critical security programs of the Department. In its first year the Office of Security Oversight has already made major contributions to strengthening the security programs of the Department. OSO has completed its reviews of all critical threat posts (44 posts in 25 countries). In FY 1991, I will continue to identify security vulnerabilities and make recommendations to improve the physical and technical security of our posts overseas. These reviews and recommendations have focused on: ensuring that security measures are consistent with threat assessments; enhancing post personnel awareness of security practices;

upgrading the physical security of facilities; updating emergency preparedness plans; and strengthening technical security countermeasures.

The Office of Investigations will continue to investigate allegations, reports, or other information indicating possible violations of law or regulation. Both the size and significance of our investigative caseload have increased, and the trend toward increased judicial actions is expected to continue, as is the sharp increase in the number of administrative actions resulting from OIG recommendations. For example, the Office of Investigations has experienced a significant increase in passport and visa fraud investigations, some of which have been conducted jointly with the Department's Bureau of Diplomatic Security. The combined efforts of these two organizations, and the steadfast support of regional security officers at U.S. missions abroad, have had significant results: three Guyanese nationals were arrested after an investigation determined that they were directly involved in selling U.S. visas to individuals who otherwise were not eligible; 16 Israeli citizens, five of whom were foreign service national employees, were arrested for their involvement in a network which sold nonimmigrant visas at prices ranging from $1,000 to $5,000 to individuals who were ineligible and, in some cases, who had been rejected previously for such visas; and in Bangkok, Thailand, investigators uncovered a highly organized network of foreign service national employees who recruited visa clients for a fee and operated their visa franchise freely within the confines of the consulate. Embezzlements and thefts, fraud against the U.S. Government, employee crimes and employee misconduct cases are also handled by our investigators.

Reports issued by our Office of Audits have recommended significant corrective action in key operations ranging from telecommunications and data processing systems to construction projects and narcotics programs overseas. During the past year we pursued savings and administrative improvements in the areas of overseas allowances and benefits, fraud prevention in consular affairs, acquisition of aviation spare parts and maintenance of computers. One audit identified internal control weaknesses leading to unnecessary costs estimated at more than $40 million annually government-wide from inflated travel per diem rates, as well as inflated differentials for hardship posts, biased education rates, questionable designation of rest and recuperation posts, and a payroll processing system that failed to charge Foreign Service employees for home leave taken. Other audit work has addressed overseas financial management; procurement and cashiering; and foreign service administrative personnel recruiting, training and assignments. We are gratified by the interest that the Congress has shown in many of these reports.

Now, I would like to turn to the areas of particular concern to the Subcommittee. In my Semiannual report to Congress last year, I identified seven areas of major management and program weaknesses that should receive priority attention from the Department. Two of the issues were security of U.S. personnel, information and facilities overseas, and international narcotics control.

I. Security of U.S. Personnel, Information and Facilities Overseas – (Antiterrorism)

As I stated earlier, our Office of Security Oversight was established in January 1989. Our security reviews have focused to date on the realism and applicability of security standards set in Washington, and the effectiveness of the Department and its posts abroad in meeting these standards. A key element of our security inspections has been to determine the vulnerability of each post to physical intrusion by terrorist attack. We have found a lack of post-specific enforceable security standards and continuing vulnerability of U.S. overseas facilities and personnel to terrorist threats. Many posts exhibited inadequate management of local guard programs, including an inordinate reliance on sole-source contracts, lack of knowledge concerning appropriate contracting procedures, and inequitable distribution of guard program costs among agencies at post.

While we have seen a general hardening of missions to the potential terrorist attack, there is always the possibility that an attack will succeed. No matter how much we devote to the problem in dollars and manpower, U.S. personnel will remain subject to an inherent risk simply by virtue of the fact that they are working overseas. Most Foreign Service Officers and personnel accept this fact as part of their job description. They know that, try as we will, we cannot ensure their safety completely. What we can try to do is to make the potential terrorist work harder. By staggering work hours, routes to work and so on, we can try to reduce somewhat the capability for a planned attack. But we cannot eliminate the possibility of an attack completely.

One of my major concerns in this whole security area is that resources are subject in many respects to the short-term focus on a particular problem. Bombings at embassies produced a new worldwide standard for delta barriers and required setbacks that have not really addressed the particular situation at our embassies. We are all focused on carbombs and physical intrusion. At many posts, particularly heretofore in East bloc countries, this is the least of our worries. And yet thousands and thousands of dollars are poured into this effort as if we can barracade ourselves against the inevitable. We must be realistic about the dangers abroad. We must assess each of these threats realistically and fashion our response appropriately. We must also do what we can, however, to ensure that the commitment to security in terms of available resources is long-term and constant.

Having completed this past year security inspections at each of the critical threat posts overseas, this office is now conducting an inspection of the overall operation of the Bureau of Diplomatic Security. An integral part of that inspection is a review of the operation of the Anti-Terrorism Assistance Program (ATA).

Depending on what we find during our current inspection of the Bureau of Diplomatic Security, we may decide that my office should conduct a more in-depth review of the ATA program, with a particular focus on whether it is meeting the intent of Congress to increase the level of antiterrorism proficiency of foreign police forces. Our detailed inspections of so many posts abroad gives us a flow of information that will complement any closer review of the ATA program. As a preliminary observation, I have noted that the Deputy Assistant Secretary for Policy and Counterterrorism position has remained vacant for approximately 18 months. To be sure, there have been acting managers, but that is a far cry from a formally appointed incumbent.

Based on our post inspections, I believe that the antiterrorism initiatives are clearly the most successful DS overseas program. The physical security of our missions, while by no means flawless, has been greatly improved in recent years, and the promulgation of uniform standards give the counterterrorism program a structure and substance that the technical security and counterintelligence disciplines still lack. DS has been professional and effective in implementing widespread security upgrades. However, missions were inspected that had been excessively upgraded with very expensive perimeter security and extensive ballistic and blast-resistant public access controls in low terrorist threat areas such as the U.S.S.R. and Eastern Europe.

However, the majority of the posts inspected lacked an environment in which officers and staff could securely create, discuss, reproduce and store classified information, principally because of a lack of emphasis on technical security programs. This failure to provide a secure working environment placed classified information and operations at risk in a number of critical and high-threat missions.

Posts were found to be generally ill-prepared to cope with emergencies, because of a lack both of preparation and of involvement in emergency preparedness by senior post management. Conversely, at missions where the ambassador took a direct and visible interest in the security program, inspection results clearly demonstrated that such high-level attention could overcome obstacles and achieve solid, effective results.

II. Refugee Assistance

We as yet do not have a completed report in this area that I can discuss with the Subcommittee. We have scheduled an inspection of the Bureau of Refugee Programs Bureau to begin in April. Our auditors also have work underway to evaluate the Department's admission process. Our audit work in this area is focused on a review of the refugee admissions program in Southeast Asia. Additionally, we will soon have the draft report of an independent CPA firm we have retained to assess the adequacy of financial accountability of selected cooperative agreements in the Bureau of Refugee Programs.

Our inspection of Embassy Bangkok last spring resulted in seven recommendations which pertain to refugee issues.

The inspectors noted that the non-government institutions (the Joint Voluntary Agencies) managing the refugee programs under grants from the U.S. Government are advocates for the same refugees. They tend to regard the refugee ceiling (the legal maximum for which funding is available) not as a ceiling but rather as a "goal" to be achieved each year. Referrals are made to INS for many who may have been economic migrants rather than political refugees.

At the time of our inspection, the Government of Thailand had expressed its concern that the likelihood of receiving refugee status and consequent subsidized immigration to the United States and other countries has encouraged a continued flow of undocumented economic migrants.

A second area of concern to the inspectors in Thailand was that the Department's agreements with the Joint Voluntary Agencies do not provide sufficient control over the organizations to the Embassy managers of these programs. Our upcoming inspection of the bureau will give us a chance to evaluate the adequacies both of the program itself and of the Department's management of the program.

III. International Narcotics Control

International narcotics control was another key area of concern which I highlighted in my Semiannual Report to Congress. My office has given considerable attention over the past two years to the Department's narcotics control activities, and will continue to do so in the future. Drug trafficking and abuse pose serious threats to the health, welfare and national security of the United States. Because most illicit drugs are cultivated and processed in foreign countries, the State Department's Bureau for International Narcotics Matters (INM) has the responsibility for international drug policy development, program management, and diplomatic initiatives. Since 1972, the Department has spent more than $660 million assisting foreign countries to combat narcotics production and trafficking within their borders.

We have published two audit reports (an Audit of Aviation Spare Parts and an Audit of INM Activities in Peru and Bolivia) and one inspection report (Inspection of the Bureau for International Narcotics Matters) in this area. We have also completed audit field work on INM programs in Pakistan, Burma, Thailand and Mexico. Draft audit reports on these programs will be issued within the next several weeks.

When I testified last July before the Subcommittee on Terrorism, Narcotics and International Operations of the Senate Foreign Relations Committee, I especially commended the dedication, courage, and professionalism of the people from the State Department (i.e., INM), DEA, Defense, other agencies, our contractors and many of the host country police and military involved in the antinarcotics mission. I noted, with some understatement, that they are carrying out a most difficult and dangerous effort. I think we owe it to them to help make sure that the support they need is not blocked or hindered back in Washington by inadequate coordination and cooperation or by bureaucratic inertia and nitpicking.

Because today's hearing is open, I will keep my comments unclassified. If the Subcommittee wishes to examine any aspects of our reports which are classified, I will be happy to address them with you in closed session.

I would like to emphasize that the information in our published reports reflects audit and inspection work completed six to 12 months ago. The Bureau, under the new leadership of the current Assistant Secretary, has agreed with most of our recommendations, and has acted aggressively to implement them. Thus, the deficiencies we found in the narcotics control area may have been corrected by now. However, I will not be sure of this until we take a second look, which is planned for later this year.

The Inspection of the Bureau for International Narcotics Matters (INM) provided additional evidence of weaknesses highlighted in earlier OIG audit and management reports. Confusion over the functional responsibilities of the bureau and lack of managerial oversight have led to deficiencies in the Department's control over efforts to stem narcotics production overseas and the flow of narcotics into the United States. Our inspection found that senior Department management has not assigned sufficient resources to meet the challenges posed by international drug trade. Although INM's budget has almost tripled since its establishment in 1986, staffing has not kept pace with its complex responsibilities. The inspectors recommended that the bureau fill existing vacancies, create new positions to meet the need, and reduce managerial confusion by more clearly delineating functional responsibilities and accountability within and among INM divisions.

The bureau's aviation support program lacks clear goals, adequate staff resources to plan and manage programs, and mechanisms to meet the aviation support needs of overseas posts carrying out narcotics control projects. INM cannot gauge the success of its aviation efforts or demonstrate that those efforts are being administered in a cost-effective and efficient manner. As a result, the program is susceptible to fraud, waste and abuse.

INM should play a more active role in coordinating intelligence collection and law enforcement activities and participate more directly in deliberations of the White House Office of National Drug Control Policy. Greater coordination is needed, both between INM and the embassies (ambassadors, narcotics coordinators, and narcotics assistance units) and within the embassies. The law enforcement agencies involved have focused more on disputes over areas of responsibility than on cooperation. The dangerous nature of many operations requires new thinking about how U.S. supported programs are to be executed, and both INM and the responsible ambassadors will have to monitor the programs more closely.

The inspection also disclosed a lack of timely and thoughtful INM reaction to narcotics program implementation plans submitted by posts. Moreover, posts tend to treat the plans as ends in themselves rather than as tools to implement and evaluate programs. The planning process needs to be refined, explained, and standardized for the bureau's domestic operations as well as overseas.

As our field work in Southeast Asia revealed, the Department does not have narcotics control programs in the countries that produce the greatest amounts of opium and heroin -- Afghanistan, Burma (INM funded programs in Burma until 1988), Iran and Laos. My auditors reviewed programs in Pakistan Burma and Thailand, where the Department has spent over $163 million since 1972. This review found several successful projects in these countries and other projects that need improvement. Our audit determined that the Department needs to:

◊ Develop a plan for a joint State Department/Agency for International Development (AID) systemic approach for planning and follow-on of narcotics-related projects;

- ◊ Use alternative strategies for crop eradication;
- ◊ Monitor law enforcement initiatives and take steps to avoid previous shortcomings;
- ◊ Monitor and evaluate the implementation of embassies' newly established procedures for more effective end-use monitoring of equipment provided to host country narcotics law enforcement agencies;
- ◊ Ensure adequate staffing at narcotics assistance units (NAUs) by establishing a management rotation plan;
- ◊ Monitor and evaluate new embassy narcotics-related reporting initiatives; and
- ◊ Monitor NAU efforts to provide oversight of suboffice operations and develop a more systemic approach to monitoring rural project sites.

While successes in reducing opium production have occurred in some countries, other countries have experienced dramatic increases in both illicit drug production and trafficking.

Our audit of INM programs in Peru and Bolivia found that despite Department-funded programs, cocoa cultivation has increased.

Mr. Chairman, this concludes my prepared statement. I would be happy to respond to questions from Members of the Subcommittee.

Mr. **Mrazek**. Thank you, Mr. Funk. I will call next on Herbert L. Beckington.

General Beckington's Opening Statement

General **Beckington**. Mr. Chairman, I am here today at the invitation of the subcommittee to testify on the subject of misuse of foreign aid.

I am a bit uncomfortable at the harshness of that title because I tend to equate the word "misuse" with deliberate misdirection or diversion or other willful misconduct by either my own agency, its agents, or the recipients of our aid.

There is some of that and we find it from time to time. But I am persuaded by the totality of my own and the GAO's reporting on our foreign economic aid program that my agency and the Congress confront a larger challenge in seeking ways to improve the effectiveness, efficiency, and, thus, the impact of our foreign aid expenditures.

That challenge, in my judgment, is to find more effective ways and procedures to deliver foreign aid than some of those that we employ and rely upon now.

In this statement, I try briefly to describe several aspects of the agency's current and long-standing procedures that I believe diminish our effectiveness, increase the vulnerability of our program performance, and create a climate that tends to invite mismanagement.

I am struck, Mr. Chairman, by the similarity of the issues that concern me and the issues that concern the GAO from my review of their witness statement. And it is not, of course, surprising that we tend to identify the same kinds of problems.

So, rather than read my entire statement, I think I will simply point out to you what those particular items are that are of concern to me, and I would do so against a background of two points. One is the extremely difficult environment in which the economic foreign aid program is carried out. I believe that my agency has one of the most severe management challenges of any agency of the Federal Government, and I identify for the committee some of those attributes of the environment in which we carry out our program.

The second point I would make, although I am constantly in the role of a critic, is that I am keenly aware of the fact that my agency, when push comes to shove, is able to perform with distinction, dedication, and competence. I give the committee a couple of examples, specific examples, of that kind of performance in the El Salvador and Jamaican natural disaster situations and in the Contra humanitarian relief program that we have administered, that my agency has administered for the last year and a half.

VULNERABILITIES IN ADMINISTERING FOREIGN AID

Now, specifically, let me discuss some of the procedures and methods that we use now and have traditionally used to deliver foreign aid that I believe make us vulnerable. First is the heavy reliance we place on third parties.

We are not a doer agency, Mr. Chairman. We don't "do" foreign aid. Foreign aid is done for us—by contractors, grantees, and host governments. This introduces an element of vulnerability right at the start.

We make heavy use of a procedure called "host country contracting," in which my agency finances a contract, from the bid through the negotiation and the award and execution process. This introduces a high degree of vulnerability in my judgment because many times, too often, these host governments are not competent, or are not able, or are not willing, or are not all three to carry out the process of contract negotiation, contract management, procurement and the financial management aspects that go with these contracts.

The second area that I touch upon very briefly is cost sharing.

Cost sharing is common in our own government, between the Federal Government and state and local governments.

The issue here for us, in the foreign aid environment, is one of commitment and sustainability. For this reason, we call upon and the statutes require a degree of cost sharing.

The problem is that the cost sharing too often does not occur. The host country either cannot or will not meet its share, which can be met either in currency or in kind, and AID either foots the bill, the project is truncated in some form or fashion, or it comes to an end and dies away, because once AID leaves, the funding is not there to carry on and to realize the benefit that was originally intended.

The third area of concern is the difficulty that we have in the handling of local currency. Local currency is an aspect of the Commodity Import Program, the PL480 Title I program, and there is frequently a local currency component in dollar cash transfers to these countries.

We have problems with local currency from the beginning to the end, and they are problems of control and accountability.

The end result is that we do not use that resource effectively.

Another area that is of concern to me, as the agency's Inspector General, is the difficulty we have in handling aid programs from the central Washington bureaus—a centrally managed program with worldwide tentacles, operating in several or sometimes many countries at once.

The agency is not well equipped and does not handle, or manage, these centrally funded programs effectively, in my judgment.

Whenever we look at one, we find serious problems. There were two recently, within the last year—the contraceptive program in connection with the agency's population planning efforts, and a major malaria research program, which was actually reviewed on a program basis by the General Accounting Office.

Finally, Mr. Chairman, I would comment on the persistence and the nagging durability of the problems which sap the vitality and effectiveness of our foreign aid program.

If you were to set aside a day and devote it to reviewing my last four or five semi-annual reports to the Congress and GAO reports over the same period that focus in any way upon issues of accountability and performance, I think you would be struck by the frequency with which the same problems emerge from this reporting.

Many factors bear on this, some not of the agency's making, such as the political and economic program environments and limits on the agency's resources. But there are issues that can be more vigorously addressed than I believe they are now or have been in the past. I have attempted to identify some of them for you this morning.

Thank you, Mr. Chairman.

[The prepared statement of General Beckington follows:]

STATEMENT OF
HERBERT L. BECKINGTON
INSPECTOR GENERAL, AGENCY FOR INTERNATIONAL DEVELOPMENT
BEFORE THE SUBCOMMITTEE ON FOREIGN OPERATIONS
OF THE
HOUSE APPROPRIATIONS COMMITTEE
MARCH 29, 1990

MR. CHAIRMAN, I AM HERE TODAY AT THE INVITATION OF THE SUBCOMMITTEE TO TESTIFY ON THE SUBJECT OF "MISUSE OF FOREIGN AID."

I AM A BIT UNCOMFORTABLE AT THE HARSHNESS OF THAT TITLE BECAUSE I TEND TO EQUATE THE WORD "MISUSE" WITH DELIBERATE MISDIRECTION OR DIVERSION OF OR OTHER WILLFUL MISCONDUCT BY EITHER MY OWN AGENCY, ITS AGENTS, OR THE RECIPIENTS OF OUR AID. THERE IS SOME OF THAT AND WE FIND IT FROM TIME TO TIME. BUT I AM PERSUADED BY THE TOTALITY OF MY OWN AND THE GAO'S REPORTING ON OUR FOREIGN ECONOMIC AID PROGRAM THAT MY AGENCY AND THE CONGRESS CONFRONT A LARGER CHALLENGE IN SEEKING WAYS TO IMPROVE THE EFFECTIVENESS, EFFICIENCY AND THUS THE IMPACT OF OUR FOREIGN AID EXPENDITURES. THAT CHALLENGE IS TO FIND MORE EFFECTIVE WAYS AND PROCEDURES TO DELIVER FOREIGN AID THAN SOME OF THOSE WE EMPLOY AND RELY ON NOW. I INTEND IN THIS STATEMENT TO BRIEFLY DESCRIBE SEVERAL ASPECTS OF THE AGENCY'S CURRENT AND LONG-STANDING PROCEDURES THAT I BELIEVE DIMINISH OUR EFFECTIVENESS, INCREASE THE VULNERABILITY OF OUR PROGRAM PERFORMANCE AND CREATE A CLIMATE THAT TENDS TO INVITE MISMANAGEMENT.

BEFORE I RAISE CERTAIN SPECIFIC ISSUES FOR YOUR CONSIDERATION I WOULD LIKE TO MAKE TWO POINTS. THEY ARE, FIRST, THE EXTREMELY DIFFICULT ENVIRONMENT IN WHICH A.I.D. MUST ROUTINELY OPERATE. I WILL ONLY TOUCH UPON THIS, MR. CHAIRMAN, BECAUSE I KNOW YOU

AND OTHER MEMBERS OF THE SUBCOMMITTEE ARE FAMILIAR WITH CONDITIONS IN THE DEVELOPING WORLD. AT A MINIMUM THEY INCLUDE:

-- A PAUCITY OF INDIGENOUS MANAGERIAL AND TECHNICAL SKILLS,

-- A LACK OF INFRASTRUCTURE SUCH AS ROADS, TRANSPORTATION SYSTEMS, RELIABLE COMMUNICATION, CLEAN WATER,

-- WEAK PUBLIC ADMINISTRATION AND FINANCIAL MANAGEMENT CAPABILITIES; AND

-- OF SIGNIFICANT IMPORTANCE, TOO FREQUENTLY, DEEPLY EMBEDDED CORRUPTION IN BOTH THE PUBLIC, AND WHERE IT EXISTS, THE PRIVATE SECTORS OF THE SOCIETY.

THE SECOND POINT I WOULD MAKE IS THAT A.I.D. HAS THE CAPACITY TO PERFORM WITH SOLID COMPETENCE, SKILL AND DEDICATION IN SITUATIONS FRAUGHT WITH RISK AND VULNERABILITY. I CITE AS EXAMPLES IN JUST THE PAST COUPLE OF YEARS THE EL SALVADOR EARTHQUAKE RELIEF AND RECONSTRUCTION EFFORT, THE JAMAICA HURRICANE RELIEF AND RECONSTRUCTION PROGRAM, AND THE NICARAGUAN HUMANITARIAN RELIEF EFFORT ASSOCIATED WITH THE CONTRAS. EACH OF THESE WERE SPECIALLY FUNDED AND HIGHLIGHTED BY THE CONGRESS AND EACH OF THEM RECEIVED SPECIAL AGENCY ATTENTION AND OVERSIGHT IN THEIR IMPLEMENTATION. OUR CLOSE SCRUTINY SHOWED NO SIGNIFICANT IMPLEMENTATION PROBLEMS.

NOW LET ME TURN TO THE SPECIFIC ISSUES THAT I BELIEVE HAMPER THE EFFECTIVENESS AND MANAGEMENT INTEGRITY OF THE AGENCY'S DAY-TO-DAY OPERATIONS. FIRST IS THE AGENCY'S HEAVY RELIANCE UPON THIRD PARTIES TO ACTUALLY DO THE WORK OF FOREIGN AID. I REFER HERE TO CONTRACTORS, GRANTEES AND HOST COUNTRIES. THIS IS A LOGICAL ELEMENT OF FOREIGN AID DELIVERY, BUT IT CARRIES WITH IT A CLEAR REQUIREMENT ON THE PART OF A.I.D. FOR CLOSE OVERSIGHT AND MONITORING OF THE ACTIVITIES AND PROGRAM

PERFORMANCE OF THESE THIRD PARTIES. TOO OFTEN THE AGENCY CANNOT OR WILL NOT EXERCISE SUFFICIENTLY CLOSE AND ATTENTIVE OVERSIGHT TO DETECT, CORRECT AND ACT UPON EMERGING PROBLEMS IN A GIVEN PROJECT OR PROGRAM AS THE PROBLEMS OCCUR OR ARE IDENTIFIED.

THE AGENCY MAKES HEAVY USE OF A DELIVERY METHOD CALLED HOST COUNTRY CONTRACTING IN WHICH A.I.D. FINANCES A CONTRACT--BID, NEGOTIATED AND AWARDED BY THE HOST COUNTRY. THIS METHOD SHOULD BE CHOSEN ONLY WHEN A.I.D. HAS DETERMINED THAT THE HOST COUNTRY HAS THE SKILLS AND EXPERTISE TO DEAL ADEQUATELY WITH ALL ASPECTS OF CONTRACT NEGOTIATION, CONTRACT ADMINISTRATION INCLUDING FINANCIAL MANAGEMENT, CONTRACT-ASSOCIATED PROCUREMENT AND MANAGEMENT OF CONTRACT-ASSOCIATED EQUIPMENT AND PROPERTIES. IN PRACTICE WE FIND THE HOST COUNTRY CONTRACTING METHOD IS TOO OFTEN CHOSEN WHEN THE HOST COUNTRY'S CAPABILITIES TO PERFORM ARE SERIOUSLY DEFICIENT AND ANY REASONABLE ASSESSMENT WOULD HAVE SO CONCLUDED AND SUGGESTED AN A.I.D. DIRECT CONTRACT APPROACH. THE VULNERABILITIES OF A.I.D. TO WASTE, FRAUD, ABUSE AND MISMANAGEMENT IN THESE CIRCUMSTANCES ARE QUICKLY APPARENT. TO COMPOUND THE RISK WE OFTEN FIND INADEQUATE A.I.D. OVERSIGHT OF THIS TYPE OF CONTRACT DURING THE LIFE OF THE CONTRACT AND WHEN THERE IS SUCH OVERSIGHT AN AWKWARDNESS IN INTERVENING IN A SITUATION IN WHICH A.I.D. IS NOT A PARTY TO THE CONTRACT. THE HOST COUNTRY CONTRACTING PROCESS IS THUS ONE METHOD OF AID DELIVERY WHICH IS FREQUENTLY USED, IS INHERENTLY FRAUGHT WITH RISK IN THE LDC ENVIRONMENT, AND THUS CARRIES WITH IT A HEAVY A.I.D. MONITORING BURDEN WHICH A.I.D. FINDS DIFFICULT OR IS RELUCTANT TO PROVIDE. OUR AID PROGRAM PAYS THE PRICE IN MANY OF THESE CASES IN SERIOUSLY FLAWED PERFORMANCE AND DISAPPOINTING RESULTS. THESE INCLUDE SIGNIFICANT DELAYS IN PROJECT IMPLEMENTATION, MILLIONS OF DOLLARS IN UNUSED OR EXCESS PROJECT EQUIPMENT, FAILURE TO ACT ON POOR CONTRACTOR PERFORMANCE OR TO EVEN MONITOR CONTRACT

PERFORMANCE AND THE DEBILITATING IMPACT OF POOR ACCOUNTING SYSTEMS AND INEFFECTIVE FINANCIAL MANAGEMENT.

ANOTHER AREA OF CONCERN IN THE PRESENT STRUCTURE OF OUR AID DELIVERY OCCURS IN COST SHARING OR HOST COUNTRY CONTRIBUTIONS. THE UNDERLYING ISSUE HERE IS SUSTAINABILITY AND HOST COUNTRY COMMITMENT. TO ENSURE THAT HOST GOVERNMENTS OR PVOS ARE COMMITTED TO THE NEED FOR A PARTICULAR PROJECT AND TO ENSURE THAT DEVELOPMENTAL EFFORT WILL CONTINUE AFTER A.I.D. FUNDING CEASES, WE REQUIRE THE HOST GOVERNMENT OR PVOS TO FORMALLY AGREE ON A SHARING OF THE COSTS OF THE DEVELOPMENTAL EFFORT. WE REPEATEDLY FIND THAT, EVEN THOUGH AGREEMENTS FORMALLY REQUIRE COST SHARING ARRANGEMENTS AND A.I.D. FAITHFULLY PROVIDES ITS AGREED-UPON SHARE, THE NON-A.I.D. SHARE NEVER MATERIALIZES. A.I.D. EITHER FOOTS THE BILL, REDUCES THE PROJECT GOALS, OR THE PROJECT DIES OR FADES AWAY WHEN A.I.D. FUNDING CEASES.

STILL ANOTHER AREA OF CONCERN IS THAT OF HOW A.I.D. DEALS WITH AND PUTS TO EFFECTIVE USE FOR DEVELOPMENTAL PURPOSES LOCAL CURRENCY. IT IS AN ISSUE THAT IS PLAGUED WITH PROBLEMS, WIDELY DEBATED, AND THE SUBJECT OF CONSIDERABLE DISAGREEMENT. THE FUNDAMENTAL ISSUE HERE IS CONTROL. ALMOST EVERY ASPECT OF OUR FOREIGN AID HAS A LOCAL CURRENCY COMPONENT. FROM OUR ECONOMIC SUPPORT FUND CASH TRANSFERS TO COMMODITY SALES UNDER ECONOMIC SUPPORT FUND AND PL 480 AGRICULTURE PROGRAMS, MILLIONS OF DOLLARS OF HOST GOVERNMENT CURRENCIES ARE PLACED ON DEPOSIT AND, IN MOST CASES, ARE TO BE USED FOR PURPOSES AGREED UPON BETWEEN THE U.S. GOVERNMENT AND THE HOST GOVERNMENT. A.I.D. SEES THESE LOCAL CURRENCIES AS A DEVELOPMENTAL TOOL AND SEEKS TO SUPPLEMENT ITS DEVELOPMENTAL EFFORTS WITH THESE RESOURCES. WE FIND PROBLEMS IN ALMOST EVERY ASPECT OF THIS PROCESS. HOST GOVERNMENTS FAIL TO MAKE DEPOSITS, IF DEPOSITS ARE MADE THEY ARE SOMETIMES YEARS LATE, DEPOSITS ARE NOT DETERMINED AT THE

HIGHEST EXCHANGE RATE AVAILABLE, DEPOSITS ARE NOT USED FOR AGREED-UPON PURPOSES, DEPOSITS ARE USED TO SUPPLANT EXISTING HOST COUNTRY RESOURCES, ETC. ONE OF THE ROOT CAUSES IN THIS TROUBLESOME AREA IS A.I.D. OPERATES WITH THE UNDERSTANDING THAT HOST GOVERNMENTS, NOT A.I.D., OWN THE LOCAL CURRENCIES ACCRUING FROM OUR AID PROGRAMS. WE MAINTAIN IT IS VERY DIFFICULT, IF NOT IMPOSSIBLE, TO CONTROL OR PROGRAM SOMETHING YOU DO NOT OWN. A.I.D. IS FREQUENTLY IN A POSITION WHERE WE HAVE LITTLE OR NO LEVERAGE TO PROGRAM THESE CURRENCIES FOR DEVELOPMENTAL PURPOSES, ACCOUNT FOR THE CURRENCIES OR IN ANY WAY CONTROL THE MANAGEMENT OF THIS RESOURCE. A.I.D. IS OFTEN BUYING LOCAL CURRENCIES WITH APPROPRIATED DOLLARS IN A COUNTRY UNDER ONE PROGRAM, WHEN EXCESS, UNUSED LOCAL CURRENCY SITS IDLE IN THE HOST GOVERNMENT'S CENTRAL BANK. FROM THE BEGINNING ACCRUAL TO THE END USE OF LOCAL CURRENCY WE CONTINUALLY FIND PROBLEMS IN WHAT WE BELIEVE IS A VALUABLE RESOURCE--IT IS REAL MONEY IN MOST OF THESE COUNTRIES. IT DERIVES IN THE FIRST INSTANCE FROM SOME ASPECT OF THE U.S. AID PROGRAM. IT IS NOT BEING EFFECTIVELY USED.

YET ANOTHER AGENCY PROCESS THAT AS PRESENTLY EMPLOYED TENDS TOO OFTEN TO ERODE THE EFFECTIVENESS AND EFFICIENCY OF OUR AID DELIVERY IS FOUND IN OUR CENTRALLY FUNDED PROGRAMS. WE DELIVER MILLIONS OF DOLLARS OF COMMODITIES, RESEARCH AND TECHNICAL SERVICES AROUND THE WORLD OUT OF THE A.I.D. OPERATING BUREAUS RIGHT HERE IN WASHINGTON, D.C. THE GLOBAL NATURE OF THESE PROGRAMS AND THE REMOTE AREAS OF THE WORLD IN WHICH WE DELIVER THEM MAKE CLOSE OVERSIGHT NEARLY IMPOSSIBLE. CONSEQUENTLY, RECENT AUDITS BY MY OFFICE AND THE GENERAL ACCOUNTING OFFICE HAVE IDENTIFIED SERIOUS PROBLEMS IN THIS MODE OF DELIVERY. A.I.D., BETWEEN 1982 AND 1988, PROCURED $244 MILLION OF CONTRACEPTIVE DEVICES. OUR AUDIT OF THE PROCUREMENT AND DISTRIBUTION OF THESE CONTRACEPTIVES FOUND THE PROGRAM TO BE SERIOUSLY FLAWED. THE GAO FOUND SIMILAR PROBLEMS IN THE CENTRALLY MANAGED MALARIA RESEARCH PROGRAM, WHERE THE AGENCY IN RECENT YEARS HAS BEEN EXPENDING ALMOST $10 MILLION ANNUALLY.

THE LACK OF GOOD FINANCIAL MANAGEMENT PRACTICES AND SYSTEMS IN THE DEVELOPING COUNTRIES HAS AN ADVERSE IMPACT ON OUR FOREIGN AID PROGRAMS. I MENTIONED THIS EARLIER IN CONNECTION WITH THE HOST COUNTRY CONTRACTING PROCESS. WE CONSISTENTLY FIND THAT HOST GOVERNMENTS AND MANY PVOS INVOLVED IN OUR PROGRAMS HAVE EXTREMELY LIMITED FINANCIAL MANAGEMENT ABILITIES AND ARE THUS PRONE TO EXPERIENCE FINANCIAL MANAGEMENT PROBLEMS THAT CAN ADVERSELY AFFECT OUR AID DELIVERY AND ACCOUNTABILITY. A.I.D.'S OWN FOCUS AS WELL AS THAT OF THE LDC'S TENDS TO BE ON OTHER MATTERS--BUILDING ROADS, IMPROVING HEALTH AND AGRICULTURE, DELIVERY OF COMMODITIES. EVEN WITHIN A.I.D. FINANCIAL MANAGEMENT PROBLEMS ARE ROUTINELY REPORTED BY MY AUDITORS. WE FIND EXCESSIVE CASH ADVANCES, UNALLOWABLE COSTS, LACK OF COST SHARING AS I NOTED EARLIER, IMPROPER OBLIGATIONS AND INACCURATE RECORDS AND REPORTING. THE NON-FEDERAL AUDIT PROGRAM, A RESPONSIBILITY OF THE INSPECTOR GENERAL BY LAW EMPLOYS CERTIFIED PUBLIC ACCOUNTING FIRMS AROUND THE WORLD TO MAKE FINANCIAL AUDITS OF INDIVIDUAL CONTRACTS AND PROJECT AGREEMENTS. WE ARE CURRENTLY OVERSEEING FOR QUALITY AND CONTENT ABOUT 100 OF THESE A YEAR, AND ONLY ABOUT ONE OUT OF FOUR ARE EXPRESSING FAVORABLE OPINIONS ON THE FINANCIAL OPERATIONS OF THE AUDITEE. THE ADVERSE IMPLICATIONS OF THIS STATISTIC FOR THE ACCOUNTABILITY AND FINANCIAL INTEGRITY OF THESE OPERATIONS SPEAKS FOR ITSELF.

FINALLY, MR. CHAIRMAN, I WOULD COMMENT ON THE PERSISTENCE, AND NAGGING DURABILITY OF THE PROBLEMS WHICH SAP THE VITALITY AND EFFECTIVENESS OF OUR FOREIGN AID PROGRAMS. IF YOU WERE TO SET ASIDE A DAY AND DEVOTE IT TO REVIEWING MY LAST FOUR OR FIVE SEMIANNUAL REPORTS TO THE CONGRESS AND GAO REPORTS OVER THE SAME PERIOD THAT FOCUS IN ANY WAY UPON ISSUES OF ACCOUNTABILITY AND PERFORMANCE I THINK YOU WOULD BE STRUCK BY THE FREQUENCY WITH WHICH THE SAME PROBLEMS EMERGE FROM THIS REPORTING. MANY FACTORS BEAR ON THIS, SOME NOT OF THE AGENCY'S MAKING SUCH AS THE POLITICAL AND ECONOMIC PROGRAM ENVIRONMENTS AND LIMITS ON

THE AGENCY'S RESOURCES. BUT THERE ARE ISSUES THAT CAN BE MORE VIGOROUSLY ADDRESSED THAN I BELIEVE THEY ARE NOW OR HAVE BEEN IN THE PAST, AND I HAVE ATTEMPTED TO IDENTIFY SOME OF THEM FOR YOU TODAY. THANK YOU, MR. CHAIRMAN.

Mr. **Mrazek**. Thank you.

I will call next on Mr. Frank C. Conahan, Assistant Comptroller General, National Security and International Affairs Division of the General Accounting Office.

Mr. Conahan.

Mr. Conahan's Opening Statement

Mr. **Conahan**. Thank you, Mr. Chairman.

I, likewise, am pleased to be here today to comment on this very important topic.

I have a rather extensive statement that I would like to present for the record, and then present a shortened version here.

My statement deals both with economic assistance and military assistance. The statement on the economic side deals with cash transfers, local currencies, contracting, procurement, items that Mr. Beckington covered.

On the military side, we talk about accountability over grant aid, technology transfers, the problems with accounting systems, and then some special program accountability issues.

Perhaps I could just highlight a few on both the economic side as well as the military side.

PROBLEMS IN ECONOMIC ASSISTANCE

Over many years, our reviews have identified management problems, internal control problems.

I must note at the outset that, though these problems continue, there have been some improvements. One improvement that I would like to take note of is the increasing accountability over cash transfers. I would like, further, to take note that that improvement was largely as a result of the efforts of this subcommittee.

I think it is important to note that AID, faced with the problem, did not move, but, rather, was forced to do some things through legislative action. I point to this committee for that effort.

I must take note, however, that even though there have been improvements in that area, we are still concerned with accountability over the cash transfer program for the reasons that AID has not yet standardized verification procedures or audit procedures over the accounts that have been established.

As Mr. Beckington pointed out, local currencies are generated by the Commodity Import Program, the PL480 program, and we, too, have noted extensive problems in control over those local currencies.

I believe that there is some debate as between the Inspector General and AID management on precisely how these funds should be handled. But, putting that aside, I think there is agreement between the Inspector General and ourselves, at least, that AID really needs to move out in this area. It just simply is not giving it the kind of attention that it requires.

Our reviews have also identified significant problems with respect to contracting overseas. The AID missions do not have control over substantial amounts of property that are in the hands of AID contractors. Also contracting procedures are deficient, particularly at the end of the contract, in terms of adequate close-out, as well as at the beginning, in terms of poor planning for procurements.

My overall statement, my prepared statement, discusses a project concerning malaria vaccine research, which really shows some poor, poor outcomes of the kind of weaknesses that I am talking about.

I also believe, as does Mr. Beckington, that these problems are systemic. We have been looking at them for a long period of time. It is disconcerting. It is frustrating to go in and find, time and time again, the same problems.

We hear over time different reasons for their existence. We have heard the same reasons that Mr. Beckington mentioned in terms of the insufficiency of staffing, the fact that they have to rely on others to do it. These have been around. If they are so systemic and if, indeed, they do impede the programs, then I believe that we all need to begin working on them more than we are doing right now.

AID recognizes these problems as part of the Financial Managers' Financial Integrity Act. They have reported them. Hopefully, this kind of increased visibility by everyone will bring about some better improvements.

PROBLEMS IN MILITARY ASSISTANCE

On the military side, the one problem that I think I would like to highlight is the difficulty in monitoring grant aid.

If you go back into the early days, we had primarily a grant aid program, and there were provisions for monitoring that program. We had large overseas military missions that did do a good job in monitoring it.

We then went to a sales program, and the question of monitoring was not on the table. We did not need to follow those things the way we did under the grant aid program.

Today, the program essentially is a grant aid program again, but the commodities are being implemented under the foreign military sales program, and there is a question out there, again, as to really how far we can go in monitoring the commodities that are being provided.

There is a case in the prepared statement dealing with the transfer, the improper transfer of fuels provided to the Government of El Salvador with military assistance financing to the enterprise that was set up supporting the Nicaraguan Contras, as well as sales back to the U.S. military.

There is a discussion in here on how we were unable, really, to trace the use of some of these funds.

It is another case of inadequate control and accountability over foreign aid on the military side.

We also looked early-on at the implementation by the Department of State of the Humanitarian Assistance Program for the Nicaraguan Contras. We found substantial problems in that program.

Since 1988, AID has taken over the administration of that program and, happily, I am able to say that they have much better control over that program than the State Department had. There are some little problems.

We recently noted some weaknesses with respect to supervision over the medical part of that, and there is some alleged criminal activity associated with it now.

In sum, I suppose I would need to say that though we have seen some improvements in the program, particularly as a result of legislative initiatives, there are still long-standing problems in both the economic, as well as the military assistance programs.

Thank you, Mr. Chairman.

[The prepared statement of Mr. Conahan follows:]

United States General Accounting Office

GAO

Testimony

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Accountability and Control Over Foreign Assistance

Statement of
Frank C. Conahan, Assistant Comptroller General
National Security & International Affairs Division

Before the Committee on Appropriations
Subcommittee on Foreign Operations, Export Financing, and Related Programs

House of Representatives

Mr. Chairman and Members of the Subcommittee:

We are pleased to be here to provide GAO's perspective on the potential for misuse of foreign economic and military aid funds. I will discuss the Agency for International Development's (AID's) accountability and control over cash transfers, its control over local currencies generated from U.S. assistance, and its management of overseas contracting and procurement systems. I will also talk about AID's malaria vaccine program, which provides a good case study of the abuses that can occur when controls are weak. Our discussions of military aid will focus on grant aid accountability, control over technology transfers, accounting systems for military aid, and the difficulties encountered in auditing covert aid. I will also discuss special program accountability issues identified in our reviews of fuel transfers to El Salvador, military aid to the Philippines, and humanitarian assistance to the Nicaraguan Democratic Resistance, or Contras.

SUMMARY OF FINDINGS

In looking at AID over the years, our reviews have identified a number of management and internal control problems. In some cases, such as with Economic Support Fund (ESF) cash transfer policy, improvements have been made in accountability based on legislative requirements for the maintenance of separate accounts for U.S. dollars. However, questions of accountability and control remain because AID's current policy for ESF cash transfers does not contain agencywide standards for verification and audit of dollar accounts.

Our reviews of Commodity Import Program (CIP) and Public Law 480 food assistance programs showed that AID could not determine whether local currency generated from the assistance was deposited, or used as required. Serious accountability issues continue to confront AID in its monitoring of local currency use. These include the lack of audit coverage for local currency accounts, poor host country reporting on account activity, and lack of assessments of host country capability to manage the accounts. Also, there is debate between AID management and the AID Inspector General over the extent to which AID, or the host-government, should maintain accountability and control over local currencies.

Our reviews of AID's overseas contracting system have also identified significant management and control weaknesses. These include (1) the lack of accountability for certain property in the hands of contractors, (2) inadequate contract close-out procedures and final audit coverage, and (3) poor procurement planning by AID's overseas missions.

A good case study of what can happen when financial accountability and internal control systems are weak is AID's malaria vaccine research project. Our review of this project found that inadequate project monitoring, lack of financial audit, and other management weaknesses directly contributed to the misuse and waste of economic assistance funds. The responsible AID project officer ultimately pled guilty to the acceptance of an illegal gratuity, and a principal university researcher was indicted for the theft of AID grant funds.

Certain problems, which increase the risk of misuse in many economic assistance programs, appear to be systemic in AID. We have found these to include limitations on AID's ability to monitor decentralized field operations, the lack of standard accountability requirements for the overseas missions, weaknesses in agency accounting and information systems, and limitations in audit coverage. AID recognizes that such problems can threaten the integrity of the program. As part of the Federal Manager's Financial Integrity Act process, AID has identified the following as material agency internal control weaknesses.

- -- A primary accounting system that has not been fully integrated with subsidiary and program systems.
- -- Inadequate audit coverage of overseas mission programs.
- -- Insufficient number of direct-hire staff.
- -- Inadequate assessments of host-country capability to manage AID-financed host country contracts.
- -- Inadequate procedures for tracking host country-owned local currency.

Our reviews of U.S. military aid have also identified a number of accountability and management problems, including

- -- limitations on U.S. monitoring of military grant aid,
- -- the unauthorized use of technology,
- -- inadequate accounting systems for management of military aid, and
- -- difficulties in auditing covert aid operations.

The case that probably best demonstrates management oversight, accountability, and control problems in military aid is the transfer of military fuels in El Salvador. We found that (1) grant aid-funded fuel supplied to the Salvadoran Air Force had been improperly transferred to air crews involved in a resupply operation supporting the Contras and (2) there were no U.S. controls over Salvadoran Air Force use of the proceeds generated from selling fuel back to the U.S. government and its contractors.

Our 1986 review of military aid to the Philippines concluded that U.S. aid was not always used or managed effectively to counter the communist insurgency in that country. We found several problems, including questionable military purchases by the Philippine military and lack of U.S. access to Philippine bases to monitor equipment use. A subsequent review indicated that some improvements had taken place.

We have also looked at the Department of State's management of humanitarian assistance for the Contras. We found that State's control procedures were insufficient to ensure that the funds were used as intended by law. Specifically, problems included State's inability to monitor and verify the validity of purchases made in the Central American region, and a limited ability to verify and monitor final delivery and use of items purchased under the program. Since 1988, AID assumed management of the Contra assistance program at the direction of the Congress.

I will now discuss these issues in more detail.

ECONOMIC ASSISTANCE

Our past and ongoing reviews of AID operations and programs have identified numerous control and management weaknesses. These weaknesses not only increase the vulnerability of AID to fraud, waste, and abuse, but also reduce the overall efficiency and effectiveness of assistance efforts. We found instances where AID could not determine if funds and commodities were used as intended. In other instances, we found that local currencies and commodities were misused.

Cash Transfers

Over the years, the United States has provided several billion dollars in ESF cash transfers as part of its assistance package.

Our reviews of ESF programs in the 1980s indicated that accountability for cash transfers was weak:

-- U.S. dollars were often commingled with other host country revenues, making accounting for these funds difficult and, in some instances, impossible.

-- Many missions relied on host countries to tell them how the money was used, instead of verifying actual use.

-- Host-country reporting on fund use was frequently late, inaccurate, or nonexistent.

For example, our 1986 report on U.S. assistance to the Philippines concluded that the disposition or actual use of over $200 million in cash transfers (provided as of February 1986) could not be determined. Special accounts were not required by AID, and ESF funds were commingled with other receipts in the Philippine Treasury. In a 1987 report on assistance to Liberia, we identified a variety of control weaknesses affecting the ESF program in the early and mid 1980s, including (1) the Liberian Government's failure to report its use of initial ESF grants, or to report within established time frames and (2) AID's failure to audit the ESF program, even though accountabilitty problems were apparent.

Legislation in effect since February 1987 requires special accounts to help track the use of ESF cash transfers. Nonetheless, we found in a review subsequent to passage of the legislation that AID still could not always trace ESF funds to their end use. Although some aid recipients we looked at (Egypt, Jamaica, and Senegal) initially deposited ESF grants into separate accounts as required, they later transferred the funds to commingled accounts before disbursing them. In some cases, however, commingling was difficult to avoid because dollars supported foreign exchange auctions or were provided to members of regional monetary unions. We also found that (1) AID's missions did not plan to systematically verify recipient reports on the use of cash transfers or audit the special accounts and (2) AID did not require separate accounts for certain types of ESF sector grants and project assistance because it did not define such assistance as cash transfers.

The most recent information available to us on the status of ESF dollar accounts is a June 1989 AID survey of its overseas missions. The AID survey developed information on both dollar and local currency accounts, including the number of such accounts, the amounts, and specific problems encountered by the missions in monitoring them. In response, the missions reported that dollar accounts had been established in commercial or federal reserve banks and that dollars were not being commingled. However, questions of accountability remain due to the lack of agencywide standards for verification and audit of dollar accounts. AID's policy on ESF cash transfers, which was established in October 1987, states that (1) assistance agreements should provide for appropriate audit, (2) recipients should periodically report on the disposition of funds, and (3) recipients should make available to

AID the records supporting their reports for 3 years after the final disbursement. AID's special account survey did not report on the extent dollar accounts have been audited.

Subsequent to AID's survey of its overseas missions, the fiscal year 1990 appropriations act for foreign operations required that separate accounts also be established by recipients of cash transfers provided as nonproject sector assistance. AID officials told us that they are now considering agencywide guidance to implement this account requirement, along with standards for verification and audit of all dollar accounts.

Local Currency Issues

As of June 1989, AID reported about 250 host country-owned local currency accounts with deposits exceeding $1 billion. Local currency is often generated from commodity and food sales and, in some cases, recipients of cash transfers are required to deposit local currency into special accounts. Our reviews of CIP and Public Law 480 food assistance programs during the 1980s concluded that inadequate accounting, monitoring, and reporting systems have prevented AID from (1) verifying that required local currency deposits were actually made and (2) determining whether withdrawals and disbursements were made for agreed purposes. Misuse of both commodities and local currency has occurred.

For example, we reported in 1987 that both Public Law 480 title I rice and local currency generated from the rice sales were misused by the Liberian Government and its agents. A several million dollar shortfall in accounts resulted. In addition, we found that the government-owned bank that managed the local currency accounts made unauthorized withdrawals of approximately $1.7 million from the fiscal year 1986 account. Our 1987 report on assistance to Indonesia also identified weaknesses in AID's accounting for the title I program. Although the problems were not nearly as serious as those in Liberia, AID did not require local currency funds to be deposited in a special account to avoid commingling, nor did it enforce Indonesian compliance with financial reporting requirements.

In 1988, we reported that the mission accounting and monitoring systems in Egypt and Pakistan--two of the largest commodity import programs--did not provide complete or accurate information on commodity imports. CIP transactions for one fiscal year were underreported by $95 million in Egypt and about $84 million in Pakistan. Without complete information on commodity transactions, AID could not identify all commodities for end use checks, or verify that required local currency deposits were made. AID monitoring of the local currency in those countries was not sufficient to provide reasonable assurance that funds were used for their intended purposes.

As previously mentioned, the June 1989 AID survey of the overseas missions provided more current information on local currency accounts. The survey indicated that significant accountability issues remain because (1) most local currency accounts had not been audited, (2) host country reporting on currency accounts was generally untimely or inaccurate, and (3) most of the missions had not assessed whether the host governments had adequate financial management systems to manage the accounts. AID missions cited the lack of staff as an obstacle in monitoring the accounts.

One issue currently being debated within AID concerns the degree of accountability and control that AID missions should exercise over local currency generated through our assistance programs. AID's management recognizes that it must have "reasonable assurance" that local currencies are used for appropriate development efforts, but it holds the host countries primarily accountable for providing adequate financial management controls because they own the funds. On the other hand, the AID Inspector General's position is that the agency must maintain control because local currency is generated from U.S. assistance. This issue has been debated for some time without being resolved, but AID officials said that they are considering several options for providing reasonable assurance that local currencies are being appropriately used. These options include (1) requiring formal and standard financial assessments of host country agencies responsible for local currency accounts and the organizations receiving the funds, (2) strengthening reporting and verification procedures for local currencies held in special accounts, and (3) requiring audits of host country agencies managing the accounts and the organizations receiving the funds.

Contracting and Procurement Issues

A significant portion of the AID program is administered through two types of contracts: direct and host country. Direct contracts are negotiated and awarded by AID, while host country contracts are negotiated and awarded by host country officials. The value of active contracts financed by AID exceeded $2 billion at the end of fiscal year 1989.

Our recently completed and ongoing reviews of AID's direct contracting system identified several internal control and management deficiencies. We found that AID does not exercise adequate accountability for project-funded nonexpendable property in the possession of contractors (for example, computer hardware and software, motor vehicles and office equipment). Also, AID was somewhat lax in ensuring that completed contracts received a final audit and were expeditiously closed out. Weak contracting and procurement management at the overseas missions, in our opinion, also contribute to internal control problems and reduced program efficiency. Potential problems identified during our ongoing review include (1) inadequate procurement planning by the missions, (2) a lack of procurement training for mission staff, particularly project officers, and (3) concerns about the independence of overseas contracting officers. Also, reliable information on AID-financed host country contracts is not available at either AID/Washington or at many of the AID missions.

The Malaria Vaccine Research Project

AID's malaria vaccine research project illustrates that U.S. programs can be subject to fraud and abuse when management, financial accountability, and internal controls are weak. AID has obligated over $90 million since 1966 for malaria vaccine research and field trial activities. Our 1989 review of this project disclosed that the project generally lacked program and financial accountability. As a result, project funds were misused or wasted. A fundamental control weakness was the lack of supervision of the malaria vaccine research project officer. The project officer and the technical office responsible for the project had misrepresented the results of pre-award evaluations of at least three research proposals and based on these misrepresentations, the proposals were selected and fully funded despite negative pre-award evaluations. We also found that competition had been waived for 10 of 11 subprojects and the basis for waiving competition was questionable in all 10 instances. Waivers had been based, in part, on inaccurate documentation sent from the technical office responsible for the malaria vaccine research project to AID procurement officials.

In addition, AID did not ensure financial audit coverage of project expenditures. Audits performed prior to 1988 focused on indirect costs and overhead rates, and did not cover direct project expenses. Consequently, these audits identified few questionable costs and uncovered no major financial management weaknesses, misuse of funds, or indications of fraud. Ours was a management review, not a fraud investigation, but it is important to note that the AID project officer ultimately pled guilty to criminal charges, including acceptance of an illegal gratuity. Also,

-- the principal researcher from the University of Hawaii was indicted for theft of AID funds;

-- University of Illinois auditors were investigating claims that the university's principal researcher had diverted AID funds to personal use; and

-- a contractor for the malaria vaccine research program has alleged that the principal researcher for a subproject at the National Institute of Health in Bogota, Colombia, defrauded the U.S. government by submitting false claims to the prime contractor.

MILITARY AID

Our reviews of U.S. military aid have identified several problems. Among these are a lack of accountability and control over aid transfers, ineffective management and use of U.S. aid by the recipient countries, and recipient transfers of items in violation of agreements governing the provision of U.S. aid and technology.

Assistance without Accountability

From the 1950s through the early 1970s, the military aid program provided U.S. equipment and services on a grant basis for use by foreign recipients. Grant aid legislation provided that items supplied under the program were subject to U.S. monitoring and control. In the 1970s, the program evolved from a grant of U.S. property to primarily a sales program. The new sales legislation was silent on authorizing U.S. monitoring. In the early 1980s, grant aid was revived as a major component of U.S. security assistance. At the Administration's request, the Congress approved administering grant aid under the sales program legislation. As a result, there is no statutory provision specifically providing for U.S. monitoring of items provided as grant aid after delivery.

This lack of U.S. legislative authority to monitor grant aid can act as a constraint on U.S. accountability over foreign aid. For example, our 1989 report on the Philippines program noted that most U.S. military aid provided to the Philippines under current foreign aid legislation becomes the property of the Philippines. The Philippine military is not required to and does not report on the distribution of this aid. Additionally, U.S. government attempts to monitor usage are dependent upon the discretion of the Philippine military to allow U.S. officials access to Philippine bases and forces. Although the access situation has improved, U.S. access to these bases and forces is still limited.

The accountability and control problem associated with monitoring foreign aid use at the discretion of the recipient is compounded by the fact that what monitoring is done is not a primary function of U.S. officials in the foreign country. While the Department of Defense (DOD) still requires monitoring, this is a secondary function for these officials. We plan to conduct a worldwide review of accountability of U.S. military aid. Among the issues to be addressed are those of constraints on U.S. accountability of equipment funded on a grant basis, the impact of national sovereignty on controls, and the trade-offs between personnel levels and accountability. The Philippines will be one of the countries included in this review.

Technology Transfers

Technology transfers is another area of increasing concern because of the potential for misuse of the technology (including that funded by U.S. foreign aid), as well as the long-term negative impact on the U.S. industrial base of unauthorized production and sales of equipment of U.S. origin. For example, our 1988 report on Korea's coproduction of the M-16 rifle disclosed that (1) Korean M-16 rifles and parts production funded with U.S. military aid exceeded levels authorized in the production agreements and (2) Korea had entered into unauthorized sales agreements with third parties, including at least one confirmed sale. These problems resulted, in part, from limited U.S. government monitoring and oversight of the program.

Our follow-up report in 1989 found similar problems. Specifically, the executive branch did not directly manage or monitor worldwide coproduction programs to ensure compliance with agreement restrictions on production quantities and third country sales. We found that unauthorized third country sales of coproduced equipment occurred in 5 of 18 major programs and in numerous minor programs. In those instances where the State Department took action regarding these violations, the typical response was a diplomatic protest.

We recommended that the Departments of State and Defense improve management controls over these transfers by adopting internal control procedures and increasing monitoring of compliance with the agreements that govern the transfers. To date, some of our recommendations have been implemented and others are in the process of being implemented.

Accounting System Problems

In addition to our reviews of the management of the provision of U.S. military aid, we have also reviewed the accounting system that supports these transfers. For over 10 years, GAO and DOD auditors have reported major accounting and internal control weaknesses that impair DOD's ability to properly manage the foreign military sales trust fund and to provide accurate statements to its customers. Additionally, these problems recently resulted in the Office of Management and Budget placing foreign military sales on its list of "high risk" areas in the federal government.

We are involved in a multi-stage review of DOD efforts to address these long-standing accounting problems. Our January 1990 report concluded that DOD has implemented enhancements to the central accounting system that are intended to ensure that records are accurate and that discrepancies between disbursements and billing records are promptly identified and corrected. We also concurred with the decision to postpone implementation of a new trust fund account until it can perform its designated function. Subsequent reports will cover the development of a new accounting and billing system for foreign military sales.

Covert Programs Hamper Auditing Controls

We are all aware of the Iran-Contra scandal. Our 1987 report on DOD's arms transfers to the Central Intelligence Agency (CIA) disclosed that DOD bypassed its normal review and approval channels in managing the arms transfers, and it underpriced the arms by $2.1 million. We recommended, in part, that DOD adjust its billing and obtain reimbursement. The CIA provided DOD with an additional payment of about $300,000 as partial reimbursement for the undercharge. CIA officials stated that this was the remainder of the funds that it had received from the third party for the sale of the missiles. Thus, the U.S. government received $1.8 million less as a result of this sale than the actual value of the missiles. In addition to the CIA role in the sale of the missiles between two agencies, GAO wanted to review the CIA's role in the overall missile transfer. However, the CIA would not allow GAO to review its role in any aspect of the Iran-Contra transfers.

We have encountered similar problems and concerns regarding the provision of aid to the Afghan rebels. In 1987 and 1989, we were requested to review the provision of military aid to the Afghan rebels, including reports of diversions and misuse of the aid. In both cases, we were not able to perform our work because the CIA would not allow us to audit a covert program. However, we were allowed to review the AID-administered Afghan assistance program. Our work confirmed our concerns about control and accountability problems associated with Afghan-related programs. Other cases that demonstrate the problems in accountability and control of military and humanitarian aid follow.

Salvadoran Fuel Transfers

In a 1989 report, we reported on allegations that U.S. military grant aid-funded fuel supplied to the Salvadoran Air Force had been improperly transferred to air crews involved in a resupply operation supporting the Contras. The State Department had been asked previously to investigate this matter and concluded that no significant diversion had occurred. I would point out that we subsequently discovered that the State investigation was fundamentally flawed. State did not question those persons with direct knowledge of the resupply operation about refueling activities.

Regarding the diversion question, we found that over $100,000 in fuel transfers to the Contras and other third parties occurred in 1986 and 1988. These transfers violated agreements between the United States and El Salvador, stipulating that title or possession of U.S.-supplied defense items or services cannot be transferred without prior U.S. government consent. Following a lengthy review of our work, the executive branch acknowledged that the diversions took place and formally notified the Congress.

We also found that the Salvadoran Air Force sold almost $1.5 million of fuel, provided on a grant basis under the U.S. military aid program, back to the U.S. government and its contractors. Sales of U.S. government-funded fuel trace back to 1985. Under the sales arrangement, the Salvadoran Air Force received local currency checks from the U.S. embassy in San Salvador for fuel transferred to U.S. military aircraft and dollar payments from contractor personnel for fuel transferred to aircraft performing work under U.S. government contracts. The use of the sales proceeds was at the discretion of the Salvadoran Air Force, with no U.S. government control or accountability over their expenditure.

Concerned about the propriety of direct payments and the lack of U.S. government control over these funds, DOD officials indicated procedures were established in April 1987 to credit U.S. fuel payments to a DOD account against future government-to-government transfers of military aid. In December 1988, we discovered that the credit system did not include the dollar payments from the contractor flights because U.S. officials had not been aware of these sales.

In June 1989 testimony on the fuel sales and the credit system, a DOD official stated, in part, that DOD had "taken appropriate steps to ensure . . . that payments received for authorized transfers are properly controlled and reutilized." Our subsequent check disclosed that this was not the case. We found that the fuel proceeds were placed in a Salvadoran account used for commercial purchases that is not reviewed or approved by the U.S. government, as the Congress and GAO had been led to believe. From April 1987 to September 1989, the Salvadoran military used the proceeds in the account to make over $1 million in commercial purchases. Among the items funded from this account were a $350,000 purchase of buildings in El Salvador, despite U.S. government concerns that the property was overvalued, and a car for the Salvadoran military attache in Washington. In addition, funds were planned for but not expended on two trips by the then Salvadoran Air Force commander. We are continuing to review the operation of this account.

I will make one final point about the fuels case. El Salvador is one of the four countries that have received fuel in recent years under the U.S. military aid program. The others are Honduras, Israel, and the Philippines. We have informally suggested to DOD officials that they review the provision of fuels to these countries to ensure that similar control and accountability problems have not occurred. While there was some agreement that this would be a prudent management practice, there has been little done to implement our suggestion. Management attentiveness of this nature could be a major factor in stopping the occurrence and continuation of problems with accountability and control.

Philippines Aid

In a 1986 report, we stated that U.S. military aid to the Philippines was not always managed or used effectively to counter the communist insurgency. Specifically, we found controversial Philippine military purchases, including one that was being investigated for fraud by the Justice Department, poor procurement planning, problems in the selection, retention, and utilization of U.S.-trained Philippine military personnel, and limited U.S. access to Philippine military installations in order to monitor how equipment was used. We noted that the United States had taken steps to reverse a general attitude that U.S. military aid was Philippine government money to be spent as it wanted, regardless of whether it addressed the primary threat.

In a 1989 follow-up report, we found that various improvements had taken place to ensure that U.S. aid was better directed toward countering the internal insurgency. Specifically, the Philippine military had improved its planning, procurement, and training. However, while U.S. officials had greater access to various Philippine bases, they were generally unable to visit the bases and operations of front line units actively engaged in the counterinsurgency program. As such, questions remain as to whether adequate control and accountability is being exercised regarding the eventual distribution of U.S. military aid.

Contra Aid

In 1985, the Congress authorized $27 million in humanitarian assistance for the Contras. A key provision of the law required the President to establish appropriate procedures to ensure that program funds were not used for other than humanitarian purposes.

We reported in 1986 that the State Department's control procedures were insufficient to ensure that the funds were used as intended by law. The State Department could not establish management controls outside the United States because certain Central American governments were unwilling to allow it to establish offices in their countries. While the State Department exercised a considerable level of control over items purchased in the United States, it could not verify the validity of purchases made in the region (64 percent of the program). State was also limited in verifying the final delivery and use of the items purchased under the program. State subsequently discovered that some payments were based on false receipts, or were for munitions, which were prohibited under the program.

About $6 million in payments for items purchased in the region were made to U.S. bank accounts of agents acting on behalf of the suppliers. State officials took the position that such payments completed the transaction between State and the suppliers, and that it had no authority to trace funds further. We disagreed with this position, since a key requirement of the authorizing legislation was the maintenance of appropriate controls to prevent misuse of the funds. Our examination of the bank account records raised several questions about the disposition of funds in the accounts. For example, we were able to trace only a small amount of the funds to specific regional suppliers, and large payments were made to the armed forces of one country.

Since 1988, when AID assumed management of the Contra assistance program at the direction of the Congress, we have observed a considerable improvement in the management of the program's operation. However, our report on the second phase of assistance pointed out that AID's medical contractor did not have a reliable system for estimating requirements for medical supplies and medicines. During the third phase, the contractor hired a subcontractor, at AID's request, to assist in developing usage rates and to handle medical procurement. We are presently reviewing these activities.

Based on a 2-year investigation by the AID Inspector General, the Justice Department has recently charged the deputy director of the AID task force in Honduras with accepting bribes from the subcontractor. The Inspector General's staff is continuing its investigation, and we are working closely with them.

Mr. Chairman, this concludes my remarks. I am available to answer any questions that you or the Subcommittee may have.

Mr. MRAZEK. Thank you, Mr. Conahan.

Finally, we will hear from Mr. Stephen Trodden, Assistant Inspector General for Auditing at the Department of Defense.

Mr. Trodden.

MR. TRODDEN'S OPENING STATEMENT

Mr. TRODDEN. Thank you, Mr. Chairman.

Like my fellow panelists, I appreciate the opportunity to be here, and with the Chair's permission, I would like to request that my prepared statement be entered into the record. I will try to summarize it at this stage.

There are basically three sections to my statement, Mr. Chairman, and then two particular problems that I raise that I think might be of particular interest to the committee.

AUDIT COVERAGE IN SECURITY ASSISTANCE

There are three general sections of the statement. The first deals with the history of our audit coverage in the security assistance area. We have previously provided staff a list of 45 audit reports that have been issued by my agency since 1982, and the statement highlights just a few of them to try to give the committee a flavor for the sort of issues that those reports have addressed. They deal with such things as supply performance by the Air Force; delays in reimbursing Air Force appropriations; stocks sold to customers that should have been reserved for Air Force needs; a Mark 46 torpedo audit that talks about overcharges, or potential overcharges, that, fortunately, we have voided to FMS customers; an audit that talked about F-18 repair parts that had not been identified for billing by the United States Navy; an audit of the European participating governments' participation in the F-16 aircraft program, which, on balance, I should inject was not a damaging report of that entire program, but did point out that there was a problem in the allocation of engineering costs to the European Governments; and an audit that we did on interest bearing accounts and the extent to which there is equity in the way interest is being allocated to the countries.

In addition to that, the statement talks about six audits that are currently in progress. One of them deals with the continuing question of the adequacy of the FMS administrative account to account for and cover all of the costs the department incurs in administering FMS programs. We are engaged now in an audit of case closures, which talks about how much trouble we seem to have in coming to closing cases with FMS countries; and an audit on the pricing and billing of technical assistance, which illustrates a deficiency in the billing of component improvement programs.

The last report that the prepared statement talks about is the Stinger missile effort, where we are currently taking a look at the accuracy of pricing and billing, and also the accountability of Stinger missiles produced since its inception.

All of this, Mr. Chairman, sort of illustrates that there are continuing problems in the FMS area. We believe that the litany of reports that my office has issued, together with that of the GAO and the service audit agencies have improved the financial management program. But still, significant problems continue to exist.

DEFENSE POLICY CHANGES

The second section of the statement comes under the rubric of major policy changes. I injected that portion into the statement, Mr. Chairman, just to make you and the committee aware of some evolving issues that the Inspector General has sort of laid on the table.

This is a draft report that is not yet final within the Department of Defense, and before these issues are finalized, I am sure there will be considerable dialogue, both within the department and between the department and the Congress on some of the matters raised in that report.

Basically, it calls into question whether or not it is time to take a look at the way we have historically done business there; whether or not such long-standing principles as "no loss" on a particular FMS transaction have simply generated a bureaucracy and an administrative nightmare in terms of our ability to deliver FMS product, and whether or not the consequence of that is a significant migration from the FMS world to the direct commercial purchase world. And there is the further question: if that is true, is it of concern to the United States?

So there are a lot of issues that are laid on the table in that report, and the statement lays them out in a little more detail

FUTURE AUDITS

The third section of my statement, Mr. Chairman, talks about where we go from here. It talks about our current process to formulate our Fiscal Year 1991 audit plan. We have some 17 audit proposals on the table at the moment.

I can assure this committee that we will give them full scrutiny and good ideas for audits from any other source as well, including this committee.

In any event, those audits will probably focus on streamlining the current accounting systems, improving pricing and billing procedures, strengthening our planning process, and developing a more responsive equipment ordering and delivery system.

Turning now, Mr. Chairman, to the two areas that I thought might be of particular interest to the committee, I would like to discuss both the FMS financing program and the Special Defense Acquisition Fund.

FMS FINANCING PROGRAM

In 1983, we made an audit of the Financial Report and Credit Program Division of the Defense Security Assistance Agency. This division is responsible for administering, accounting, and reporting for the FMS financing program.

The resultant audit report contained a finding that recommended a definitive policy as to the types of items that could be purchased with these funds. The auditors identified some procurements that appeared to be, to them, more of economic assistance than security assistance, and also a lack of specific procedures to be followed in approving commercial sales financed with FMS credits.

Subsequent to that audit, a contract was found to contain a kickback arrangement between the contractor and the subcontractor. As a result, the then-current Defense Inspector General, Mr. Sherick, sent a memorandum to the Under Secretary of Defense for Policy that called for tighter controls over direct commercial purchases.

In 1985, the DSAA established a requirement that did provide audit access to these contracts, down to the subcontractor level.

Over the past few years, DSAA has requested the Defense Contract Audit Agency to audit a number of these credit financed procurements. The primary purpose of these audits has been to determine whether the requirement for the procurement of materials of U.S. origin has been complied with.

In July of this past year, we started an audit of direct commercial sales financed with FMS credits. The purpose of this audit is to determine whether the internal controls that the DSAA has in place are complete and whether they are working.

We are nearing the completion of this audit, and I would like to share some tentative observations.

During the audit, we visited eight contractors. We were looking to see whether a fair price was obtained. In some cases, there was a lack of support for the negotiated price, and in one case, the negotiated profit appeared to exceed the profit that the contractor would have been entitled to had it been a DOD procurement.

Although we have not yet discussed our results inside the department nor with the assistance agency, we have identified a need for better pricing analysis prior to approval of credit financing.

It should be noted that this audit originally intended to include direct commercial sales financed for the Government of Israel. Shortly after we started the audit, the GAO announced that they were going to review the operations of the Israeli Buying Office, and so, we downscoped our job to recognize the GAO job.

For reasons of their own, the GAO has also had to postpone this effort, and, therefore, I would submit that this is a program area requiring coverage in the near future. We will be working with the GAO planners to make sure that area is picked up by one of us.

Last month, the Comptroller of the Defense Security Assistance Agency approached me—and he is a new Comptroller—about the implementation of legislation that requires DOD to audit contracts selected by his agency. I will confess to this committee that I had been unaware of this legislative requirement, and the Defense Inspector General is now working on an audit policy that will provide the audit coverage that this committee desires.

Tentatively, I would submit that it would seem to make sense that the Defense Contract Audit Agency be involved, as they are in all matters of defense procurement, in performing pre-award pricing type audits and possibly post-award defective pricing type audits—although the application of the Truth in Negotiation Act to such procurements is questionable.

My agency, I believe, should be involved in future audits of the type that we are now doing that look at the entire systemic issue surrounding the agency's involvement in the credit financing program.

I recognize that the existing legislation does not preclude us from performing such systemic audits. But it may be appropriate to clarify the legislation as to the depth and quantity of contract auditing that the committee had in mind when the existing legislation was adopted.

I am prepared on behalf of the Defense Inspector General to commit us to periodic systemic audits on this program.

SPECIAL DEFENSE ACQUISITION FUND

The second subject that I thought should be addressed is the Special Defense Acquisition Fund.

In 1985, the GAO issued a report on this area. They concluded that it was too early to state whether the objectives of the fund would be accomplished. However, they did observe that reduced delivery time had been achieved.

GAO recommended that Congress allow obligation authority with a three-year life be made available to the fund.

My own office made an audit of the Special Defense Acquisition Fund in 1986. Our objective was to evaluate controls over both appropriated funds and physical assets belonging to the fund.

We evaluated procedures for pricing and billing and determined if procurements made by the fund met the objectives for which the fund was established.

We reported on September 15, 1987, that substantial improvements in the management and accounting for the fund were needed. The financial procedures did not provide proper billing and delivery reporting to customers, and charges to the fund did not include all costs, such as civilian retirement and the cost of military labor.

Due to the magnitude of the problems disclosed, we announced on February 27 of this year that we will audit the fund again, and this audit will include the same objectives of our prior audit.

This concludes my testimony, Mr. Chairman.

In summary, I believe we have made some significant contributions to the better management of this program. I can assure this committee that we will continue to give this area significant coverage. We will pay particular attention to establishing a more responsive system for managing FMS, for providing oversight of U.S. financing of direct commercial sales, and good suggestions from all sources, including this committee.

Again, Mr. Chairman, I appreciate the opportunity to be here and I am now willing to answer any questions you or members of the committee may have.

Thank you.

[The prepared statement of Mr. Trodden follows:]

STATEMENT

MR. STEPHEN A. TRODDEN
ASSISTANT INSPECTOR GENERAL FOR AUDITING
OFFICE OF THE INSPECTOR GENERAL
DEPARTMENT OF DEFENSE

BEFORE THE
SUBCOMMITTEE ON FOREIGN OPERATIONS, EXPORT FINANCING
AND RELATED PROGRAMS
COMMITTEE ON APPROPRIATIONS
UNITED STATES HOUSE OF REPRESENTATIVES
101ST CONGRESS, SECOND SESSION

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U.S. HOUSE OF REPRESENTATIVES

MR. CHAIRMAN AND MEMBERS OF THE COMMITTEE, I WOULD LIKE TO THANK YOU FOR THE OPPORTUNITY TO APPEAR TODAY ON BEHALF OF THE DEFENSE INSPECTOR GENERAL TO DISCUSS THE AUDIT WORK WE HAVE DONE IN THE SECURITY ASSISTANCE PROGRAM. MY STATEMENT HAS THREE PRINCIPAL PARTS:

- LESSONS LEARNED FROM PAST AND ONGOING AUDIT EFFORTS;

- MAJOR POLICY RECOMMENDATIONS DEVELOPED BY THE OIG; AND,

- WHAT WE ARE CURRENTLY PLANNING FOR THE FUTURE.

LESSONS LEARNED

SINCE FISCAL YEAR 1982, WE HAVE ISSUED 45 AUDIT REPORTS THAT RELATE TO SECURITY ASSISTANCE. A LIST OF THE AUDIT REPORTS HAS BEEN PROVIDED TO THE COMMITTEE. OUR WORK IN SECURITY ASSISTANCE HAS CONCENTRATED ON THE FOREIGN MILITARY SALES PROGRAM, WHICH HAS HAD A MULTITUDE OF PROBLEMS. FOR EXAMPLE:

- OUR AUDIT OF THE FMS SUPPLY PERFORMANCE BY THE AIR FORCE SHOWED THAT DELAYS WERE INCURRED IN REIMBURSING AIR FORCE APPROPRIATIONS FOR SUPPLIES SOLD AND FOREIGN CUSTOMERS WERE SOLD SUPPLIES FROM STOCKS THAT SHOULD HAVE BEEN RESERVED FOR AIR FORCE REQUIREMENTS;

- OUR AUDIT OF THE MK-46 TORPEDO IDENTIFIED CONTRACTING PRICING IRREGULARITIES THAT, IF LEFT UNCORRECTED, WOULD HAVE RESULTED IN OVERCHARGES TO FMS CUSTOMERS OF ABOUT $10 MILLION;

- OUR AUDIT OF FOREIGN MILITARY SALES PERFORMANCE BY THE NAVY IDENTIFIED 52 SHIPMENTS OF F-18 REPAIR PARTS, VALUED AT $1.4 MILLION, THAT THE NAVY HAD NOT IDENTIFIED FOR BILLING TO FOREIGN CUSTOMERS;

- OUR AUDIT OF THE PRICING AND BILLING OF THE F-16 AIRCRAFT SHOWED THAT WHILE THE AIR FORCE HAD DONE A GOOD JOB OF MANAGING AND ADMINISTERING THIS $5.4 BILLION PROGRAM, THE EUROPEAN PARTICIPATING GOVERNMENTS WERE NOT BILLED FOR THEIR FAIR SHARE OF ENGINEERING CHANGE PROPOSALS ESTIMATED TO BE $9.7 MILLION; AND,

- OUR AUDIT OF THE DRAWDOWN PROCEDURES ON INTEREST-BEARING ACCOUNTS SHOWED THAT FIVE COUNTRIES THAT RECEIVED CREDIT FINANCING WERE INAPPROPRIATELY ALLOWED TO EARN ABOUT $24 MILLION A YEAR IN INTEREST, WHILE OTHER COUNTRIES WERE IMPROPERLY DENIED INTEREST EARNINGS.

WE CURRENTLY HAVE SIX AUDITS IN PROGRESS. THESE INCLUDE:

- AN AUDIT OF THE FMS ADMINISTRATIVE ACCOUNT THAT SHOWS THAT THE EXPENSES LEVIED AGAINST THIS ACCOUNT FOR THE COSTS OF ADMINISTERING THE PROGRAM HAVE OUTPACED THE REVENUES;

- AN AUDIT OF THE CASE CLOSURE PROCEDURES FOR FOREIGN MILITARY SALES WHICH SHOWS THAT CLOSURES ARE BEING DELAYED SEVERAL YEARS AFTER SUPPLIES OR SERVICES WERE PROVIDED;

- AN AUDIT ON THE PRICING AND BILLING OF TECHNICAL ASSISTANCE SOLD TO FMS CUSTOMERS WHICH SHOWS A SIGNIFICANT DEFICIENCY IN THE BILLING OF COMPONENT IMPROVEMENT PROGRAMS FOR AIRCRAFT ENGINES; AND,

- AN AUDIT TO DETERMINE WHETHER STINGER MISSILES SOLD TO FOREIGN CUSTOMERS ARE ACCURATELY PRICED AND BILLED AND WHETHER THERE IS ACCOUNTABILITY FOR THE MISSILES PRODUCED.

EVEN THOUGH THE FMS PROGRAM SUFFERS FROM A MYRIAD OF FINANCIAL, ADMINISTRATIVE, AND PROCEDURAL PROBLEMS WE BELIEVE THE PROGRAM IS IN BETTER SHAPE TODAY AS A RESULT OF OUR AUDIT ACTIVITIES. WHILE DOD MANAGEMENT HAS TAKEN CORRECTIVE ACTION ON SPECIFIC RECOMMENDATIONS MADE IN OUR AUDIT REPORTS WE BELIEVE SYSTEMIC PROBLEMS STILL EXIST. FOR EXAMPLE, THERE IS A CONTINUATION OF MANY OF THE CONCERNS THAT WE HAVE BEEN FACED WITH OVER THE YEARS, SUCH AS HAVING TO USE APPROPRIATED FUNDS TO SUBSIDIZE FOREIGN MILITARY SALES, AND MORE RECENT CONCERNS THAT FOREIGN BUYERS ARE TURNING TO COMMERCIAL SALES TO AVOID THE COSTLY AND BURDENSOME BUREAUCRATIC SYSTEM FOR MANAGING FOREIGN MILITARY SALES. WHILE IT HAS ADMITTEDLY TAKEN US SOME TIME, WE HAVE COME TO THE CONCLUSION THAT CORRECTING MANY OF THESE PROBLEMS MAY REQUIRE SOME MAJOR CHANGES TO THE FMS PROGRAM.

MAJOR POLICY CHANGES

IN ORDER TO BRING THE OVERALL MANAGEMENT OF THE FMS PROGRAM INTO FOCUS THE DOD, OIG CONDUCTED A BROAD-BASED INSPECTION OF THE SECURITY ASSISTANCE PROGRAM. A REPORT ON THE INSPECTION THAT I AM REFERRING TO IS IN DRAFT AND IT IS CURRENTLY BEING STAFFED WITH DOD MANAGEMENT. WE EXPECT TO ISSUE THE FINAL REPORT WITHIN THE NEXT TWO MONTHS. HOWEVER, I CAN GIVE YOU TENTATIVE RESULTS.

THE INSPECTION REVEALED THAT SECURITY ASSISTANCE SUFFERS FROM A MORASS OF ADMINISTRATIVE PROCEDURES DESIGNED TO MEET THE LEGISLATIVELY MANDATED "NO-LOSS" PRINCIPLE FOR SELLING MILITARY EQUIPMENT ON A CASE-BY-CASE BASIS. THE INSPECTION REPORT POINTS OUT THAT THIS PRINCIPLE FORCES DOD ELEMENTS TO PERFORM UNNECESSARILY DETAILED ACCOUNTING, AND PRECLUDES THE IMPLEMENTATION OF BUSINESS PRACTICES THAT WOULD ALLOW THE FMS PROGRAM TO COMPETE MORE FAVORABLY WITH DIRECT COMMERCIAL SALES AND FOREIGN SUPPLIERS.

SOME OF THE THE MAJOR POLICY INITIATIVES ADDRESSED IN THIS REPORT INCLUDE:

- REVISING THE "NO-LOSS NO-GAIN" CONCEPT TO FOCUS ON A SYSTEM THAT WOULD BREAK-EVEN OVER THE LONG TERM RATHER THAN ON A CASE-BY-CASE BASIS;

- SIMPLIFYING THE COMPLEX FMS ORDER AND DELIVERY SYSTEM;

- CORRECTING FLAWS IN THE FMS ACCOUNTING SYSTEM WHICH HAVE RESULTED IN AN OUT-OF-BALANCE SITUATION IN THE TRUST FUND; AND,

- EXPANDING OVERSIGHT OF DIRECT COMMERCIAL SALES SO THAT FMS AND DIRECT SALES ARE VIEWED AS TWO COMPONENTS OF ONE NATIONAL POLICY.

WHILE I BELIEVE THESE INITIATIVES ARE A STEP IN THE RIGHT DIRECTION, THERE IS MUCH MORE WE NEED TO DO WITH RESPECT TO DETERMINING THE MOST EFFECTIVE AND ECONOMICAL WAY TO ACHIEVE THESE REFORMS. IMPROVING THE SECURITY ASSISTANCE PROGRAM WILL REQUIRE MORE THAN JUST OVERSIGHT. IT WILL REQUIRE INTERNAL DOD ACTION, COORDINATION WITH OTHER EXECUTIVE DEPARTMENTS, AND CONGRESSIONAL SUPPORT.

FUTURE EMPHASIS

THIS INSPECTION REPORT, COUPLED WITH OUR PAST AND ONGOING AUDIT EFFORTS, HAS SET THE FOUNDATION FOR A NEW WAY OF THINKING WITH RESPECT TO PLANNING AND FOCUSING OUR AUDIT RESOURCES IN THE AREA OF SECURITY ASSISTANCE. THE RESULTS OF THIS WORK WILL ASSIST IN BRINGING ABOUT MAJOR IMPROVEMENTS IN THE WAY WE USE SECURITY ASSISTANCE AS AN INSTRUMENT OF NATIONAL SECURITY POLICY.

WE ARE CURRENTLY DEVELOPING OUR FISCAL YEAR 1991 AUDIT PLAN. THUS FAR WE HAVE IDENTIFIED 17 AUDITS INVOLVING SECURITY ASSISTANCE. IN PRIORITIZING THESE AUDITS WE WILL CONTINUE TO DO MANY OF THE SAME TYPE OF ECONOMY AND EFFICIENCY AUDITS THAT WE HAVE DONE IN THE PAST. WE WILL ALSO USE THIS PLANNING PROCESS TO ENCOMPASS SOME OF THE INITIATIVES OUTLINED IN THE INSPECTION REPORT. OUR AUDITS WILL FOCUS ON:

- STREAMLINING CUMBERSOME ACCOUNTING SYSTEMS;

- IMPROVING PRICING AND BILLING PROCEDURES;

- STRENGTHENING THE PLANNING PROCESS; AND,

- DEVELOPING A MORE RESPONSIVE EQUIPMENT ORDERING AND DELIVERY SYSTEM.

BEFORE I CONCLUDE MY TESTIMONY, I WOULD LIKE TO DISCUSS TWO SECURITY ASSISTANCE PROGRAMS THAT ARE DIRECTLY SUPPORTED BY APPROPRIATED FUNDS; THE FMS FINANCING PROGRAM AND THE SPECIAL DEFENSE ACQUISITION FUND.

IN 1983, WE MADE AN AUDIT OF THE FINANCIAL REPORT AND CREDIT PROGRAM DIVISION OF THE DEFENSE SECURITY ASSISTANCE AGENCY. THIS DIVISION IS RESPONSIBLE FOR ADMINISTERING, ACCOUNTING AND REPORTING FOR THE FMS FINANCING PROGRAM. THE RESULTANT AUDIT REPORT CONTAINED A FINDING THAT RECOMMENDED A DEFINITIVE POLICY

AS TO THE TYPES OF ITEMS THAT COULD BE PURCHASED WITH THESE FUNDS. THE AUDITORS IDENTIFIED PROCUREMENTS THAT APPEARED TO BE MORE OF ECONOMIC ASSISTANCE RATHER THAN SECURITY ASSISTANCE. WE ALSO IDENTIFIED A LACK OF SPECIFIC PROCEDURES TO BE FOLLOWED IN APPROVING COMMERCIAL SALES FINANCED WITH FMS CREDITS.

SUBSEQUENT TO THIS AUDIT, A CONTRACT WAS FOUND TO CONTAIN A KICKBACK ARRANGEMENT BETWEEN THE CONTRACTOR AND A SUBCONTRACTOR. AS A RESULT OF THIS CONTRACT, THE INSPECTOR GENERAL, MR. SHERICK, SENT A MEMORANDUM TO THE UNDER SECRETARY OF DEFENSE FOR POLICY ON MAY 2, 1985 THAT CALLED FOR TIGHTER CONTROLS OVER DIRECT COMMERCIAL PURCHASES. IN 1985, THE DEFENSE SECURITY ASSISTANCE AGENCY ESTABLISHED A REQUIREMENT THAT PROVIDED AUDIT ACCESS TO THESE CONTRACTS DOWN TO THE SUBCONTRACTOR LEVELS.

OVER THE PAST FEW YEARS, THE DEFENSE SECURITY ASSISTANCE AGENCY HAS REQUESTED THE DEFENSE CONTRACT AUDIT AGENCY TO AUDIT A NUMBER OF THESE FINANCED PROCUREMENTS. THE PRIMARY PURPOSE OF THESE AUDITS HAS BEEN TO DETERMINE WHETHER THE REQUIREMENT FOR THE PROCUREMENT OF MATERIALS OF U.S. ORIGIN HAS BEEN COMPLIED WITH.

IN JULY OF LAST YEAR, WE STARTED AN AUDIT OF DIRECT COMMERCIAL SALES FINANCED WITH FMS CREDITS. THE PURPOSE OF THIS AUDIT IS TO DETERMINE WHETHER THE INTERNAL CONTROLS THE DEFENSE SECURITY ASSISTANCE AGENCY HAS IN PLACE ARE COMPLETE AND ARE

WORKING. WE ARE NEARING THE COMPLETION OF THIS AUDIT AND I WOULD LIKE TO SHARE SOME OF OUR OBSERVATIONS. DURING THE AUDIT, WE VISITED EIGHT CONTRACTORS. THE PRIMARY PURPOSE OF THE VISITS WAS TO DETERMINE WHETHER A FAIR PRICE WAS OBTAINED. IN SOME CASES, THERE WAS A LACK OF SUPPORT FOR THE NEGOTIATED PRICE. IN ONE CASE, THE CONTRACTOR'S PROFIT APPEARED TO EXCEED THE PROFIT HE WOULD HAVE BEEN ENTITLED TO IF IT WERE A DOD PROCUREMENT. ALTHOUGH WE HAVE NOT YET DISCUSSED OUR RESULTS WITH THE DEFENSE SECURITY ASSISTANCE AGENCY, WE HAVE IDENTIFIED A NEED FOR BETTER PRICING ANALYSIS PRIOR TO APPROVAL OF CREDIT FINANCING.

IT SHOULD BE NOTED THAT THIS AUDIT ORIGINALLY INTENDED TO INCLUDE DIRECT COMMERCIAL SALES FINANCED FOR THE GOVERNMENT OF ISRAEL. SHORTLY AFTER WE STARTED THIS AUDIT, THE GENERAL ACCOUNTING OFFICE ANNOUNCED THAT THEY WERE GOING TO REVIEW THE OPERATIONS OF THE ISRAELI BUYING OFFICE THAT USES PROGRAM FUNDS TO FINANCE THEIR COMMERCIAL PURCHASES. IN ORDER TO AVOID DUPLICATION OF AUDIT EFFORT, WE EXCLUDED THE ISRAELI PROGRAM FROM OUR AUDIT. THE GENERAL ACCOUNTING OFFICE LATER DECIDED TO TERMINATE ALL WORK CONCERNING THIS PROGRAM. SUBSEQUENTLY, THIS REMAINS A MAJOR ISSUE REQUIRING COVERAGE. WE WILL WORK WITH THE GENERAL ACCOUNTING OFFICE IN THE DEVELOPMENT OF OUR FISCAL YEAR 1991 AUDIT PLAN TO PROVIDE ADEQUATE COVERAGE OF THIS AREA.

LAST MONTH, THE COMPTROLLER OF THE DEFENSE SECURITY ASSISTANCE AGENCY APPROACHED ME ABOUT THE IMPLEMENTATION OF THE LEGISLATION THAT REQUIRES DOD TO AUDIT CONTRACTS SELECTED BY THE

DEFENSE SECURITY ASSISTANCE AGENCY. I ADMIT WE HAD MISSED THIS LEGISLATIVE REQUIREMENT AND WE ARE NOW WORKING ON AN AUDIT POLICY THAT WILL PROVIDE THE AUDIT COVERAGE THIS COMMITTEE DESIRES. I BELIEVE THAT THE DEFENSE CONTRACT AUDIT AGENCY SHOULD BE INVOLVED IN PERFORMING PREAWARD PRICING TYPE AUDITS AND POSSIBLY POST AWARD DEFECTIVE PRICING TYPE AUDITS. WE SHOULD BE INVOLVED IN AUDITS THAT INVOLVE SYSTEMIC PROBLEMS THAT COVER THE ENTIRE PROCESS. WHILE WE RECOGNIZE THAT THE EXISTING LEGISLATION DOES NOT PRECLUDE US FROM PERFORMING SUCH SYSTEMIC AUDITS, IT MAY BE APPROPRIATE TO CLARIFY THE LEGISLATION AS TO THE DEPTH AND QUANTITY OF CONTRACT AUDITS DESIRED. I AM PREPARED TO COMMIT THE DOD, OIG TO PERIODIC PERFORMANCE OF SYSTEMIC AUDITS ON THIS PROGRAM.

IN 1985, THE U.S. GENERAL ACCOUNTING OFFICE ISSUED A REPORT ON THE DESIGN AND OPERATION OF THE SPECIAL DEFENSE ACQUISITION FUND. GAO REPORTED THAT IT WAS TOO EARLY TO CONCLUDE WHETHER THE OBJECTIVES OF THE FUND WOULD BE ACCOMPLISHED. HOWEVER, THE USE OF THE FUND HAS RESULTED IN REDUCED DELIVERY TIME ON FOREIGN MILITARY SALES. GAO RECOMMENDED THAT CONGRESS ALLOW 3-YEAR OBLIGATION AUTHORITY FOR AMOUNTS MADE AVAILABLE TO THE FUND.

WE MADE AN AUDIT OF THE SPECIAL DEFENSE ACQUISITION FUND IN 1986. THE OBJECTIVE OF THIS AUDIT WAS TO EVALUATE CONTROLS OVER APPROPRIATED FUNDS AND PHYSICAL ASSETS. WE ALSO EVALUATED THE PROCEDURES FOR PRICING AND BILLING MATERIEL DELIVERED FROM THE FUND AND DETERMINED IF PROCUREMENTS MADE BY THE FUND MET THE

OBJECTIVES FOR WHICH THE FUND WAS ESTABLISHED. WE REPORTED ON SEPTEMBER 15, 1987, THAT SUBSTANTIAL IMPROVEMENTS IN THE MANAGEMENT AND ACCOUNTING FOR THE FUND WERE NEEDED. THE FINANCIAL PROCEDURES DID NOT PROVIDE PROPER BILLING AND DELIVERY REPORTING TO CUSTOMERS, AND CHARGES TO THE FUND DID NOT INCLUDE ALL COSTS SUCH AS CIVILIAN RETIREMENT AND MILITARY LABOR. DUE TO THE MAGNITUDE OF THE PROBLEMS DISCLOSED, WE ANNOUNCED ON FEBRUARY 27, 1990, THAT WE WOULD AUDIT THE FUND AGAIN. THIS AUDIT WILL INCLUDE THE SAME OBJECTIVES OF OUR PRIOR AUDIT.

SUMMARY

THIS CONCLUDES MY TESTIMONY. I BELIEVE WE HAVE MADE SOME SIGNIFICANT CONTRIBUTIONS TO BETTER MANAGEMENT OF THE PROGRAM. I CAN ASSURE THIS COMMITTEE THAT WE WILL CONTINUE TO GIVE THIS AREA SIGNIFICANT COVERAGE. WE WILL PAY PARTICULAR ATTENTION TO ESTABLISHING A MORE RESPONSIVE SYSTEM FOR MANAGING FOREIGN MILITARY SALES, PROVIDING OVERSIGHT OF U.S. FINANCING OF DIRECT COMMERCIAL SALES, AND GOOD SUGGESTIONS FROM ALL SOURCES, INCLUDING THIS COMMITTEE. AGAIN MR. CHAIRMAN, I APPRECIATE THE OPPORTUNITY TO BE HERE AND I AM NOW WILLING TO ANSWER ANY QUESTIONS YOU OR MEMBERS OF THE COMMITTEE MAY HAVE.

Mr. **Mrazek**. Thank you very much, Mr. Trodden.

I appreciated the breadth of the testimony. It is certainly very helpful with respect to pointing out directions that we need to explore a little more carefully.

INTERNATIONAL NARCOTICS CONTROL: PERU AND BOLIVIA

I would like to first ask you, Mr. Funk, about the audit that you did on the International Narcotics Control Programs in Peru and Bolivia.

I would just quote from one conclusion that you drew in that report, when you said that the INM funded programs in Peru and Bolivia, "Have not resulted in significant reductions of coca cultivation or the disruption of the cocaine trafficking in the host countries. Coca production in those countries has increased every year, and less than 1 percent of the illicit drugs has been seized. It is uncertain whether INM funded programs, as they are now conducted, will have a meaningful impact on the amount of cocaine that is available for export."

"The INM programs, besides being ineffective, are also unnecessarily dangerous, are implemented in ways that detract from program objectives, and waste Federal funds."

That is quite harsh with respect to that particular program.

I am curious to know whether you are essentially precluded, in your own mind, from looking at whether the strategies being employed represent appropriate policy, or whether you are looking at individual trees, rather than the forest, with respect to these programs.

Mr. **Funk**. Mr. Chairman, the forest is now a new ballgame. Of course, there is a National Drug Strategy that has been articulated by the President and by Mr. Bennett. Whether or not that strategy is being translated into effective programs at the operating level can only be determined at that level.

As IGs, we are not supposed to be in the position of questioning broad policy. We are supposed to be looking at whether programs work.

So, indeed, we are going to look, and are looking, at whether or not there has been an improvement in Peru and Bolivia, an improvement in some of the states of Southeast Asia.

Our difficulties are many. One difficulty is that we have no drug control programs in the greatest poppy and opium producing areas in Asia—Iran, Afghanistan and Burma. Burma has been closed to us since 1988. That is where much of the stuff comes from, where much of the heroin comes from.

We have no programs there at all.

I mentioned before the turf fights. I would hope, profoundly hope, that Mr. Bennett's National Drug Office is, in fact, going to pull these things together.

I have to tell you that we looked at this thing in Peru and Bolivia a year ago. We are going back for a second look again, to see whether or not there has been an improvement. I think some of the problems have been corrected. The situation is not as dangerous as it was before. INM has significantly beefed up the capability of the local military.

Remember, sir, we do not fight these wars, these drug wars, overseas. We are simply the funding agency. The United States is totally at the discretion of the host government, the military of the host government and the police. We can guide, we can lead, we can point, but we cannot do. That is something the United States Government cannot handle.

So my overall answer to you would be it is not proven yet one way or the other. All of the data that comes out about hectares eliminated of coca or poppies remind me, frankly, of the body count in Vietnam. The Defense Department must play an increasing role. It was a reluctant virgin until fairly recently. But Defense is coming on now very strong and very hard.

So I am a bit more sanguine than I was before. But it remains to be proven, sir.

Mr. **Mrazek**. You outline in your audit on page four about 16 different major weaknesses that seem pretty comprehensive and overwhelming in terms of making improvements in the program.

Now you're going to go back in, after another year. We're spending tens of millions of dollars on a program to eradicate coca plants in these countries. In Bolivia, we are doing it with the ostensible cooperation of the Bolivian Government. And we are eradicating 1 percent you say in your audit of the coca being produced.

I don't know how you can suggest that you plan to go back and hope to see significant improvement.

Mr. **Funk**. Well, the introduction of Defense will be a new factor. Defense was not really involved to any significant extent a year ago.

When we go back now, we are really talking about paramilitary operations. By any name, that is what they are. That is not DEA's "primary bag."

Well, Defense I would certainly hope is expert in that area. They have a much stronger commitment now.

Will it end up by showing that we have a lot of input but no output? That remains to be seen.

We can control the input. But, obviously, the output leaves something to be desired.

I have to tell you that I am more sanguine, yes. INM has its act together better than it was before. I believe that DEA is training its people better. They speak Spanish now. Previously, the agents could not even speak Spanish.

Mr. **Mrazek**. That would seem to be a rather crippling difficulty.

Mr. **Funk**. Yes, sir.

I have some reservations. The quality of arms that the people have for defensive work leaves something to be desired. There are a number of other major difficulties.

But, again, we have a strong push from on top, and sometimes that push from on top can work wonders.

In terms of the Scottish judicial verdict, I have to say that right now it is not "proven."

STATE DEPARTMENT PRIORITY FOR INM

Mr. **Mrazek**. Well, I don't know, based on reading your report, it would seem to me that the senior leadership of the State Department has not really assigned a very high priority to this effort. You talk about the need for bringing in the Defense team. But I am curious as to what the State Department is doing with respect to fixing these programs so that we are not wasting the tens of millions of dollars that they are spending.

Mr. **Funk**. In this case, there has been a significant improvement.

A year ago, we found very little signs of a high priority. When we did the inspection last summer of the Bureau of International Narcotics Matters, we found too where there had not been that kind of priority given to it.

Since then, I have to tell you, sir, that the Secretary, the Deputy Secretary, Larry Eagleburger, and Melvin Levitsky, who is the Assistant Secretary for International Narcotics, have been given more resources, which is the acid test of any kind of priority in government. They have gotten more resources.

The Bennett proposal is putting $50 million more into the Andean strategy than was the case before.

Mr. **Mrazek**. Into the what?

Mr. **Funk**. Into the Andean strategy, for Peru, Bolivia, and Colombia, to do a better job of eradication and interdiction.

Whether it can ever be solved at the supply level, again, sir, that is not proven. But the priority is there, now, in terms of State Department.

I could not say that a year ago. I could not even say it six months ago. But I can say it now. They are getting priority here.

Mr. **Lewis**. Mr. Chairman, may I ask a question?

Mr. **Mrazek**. Yes.

Mr. **Lewis**. The report relative to countries like Bolivia, how old is that report?

Mr. **Funk**. A year ago. The field work was done almost exactly a year ago.

Mr. **Lewis**. Have there been significant changes since then?

Mr. **Funk**. On the management side, yes, sir. The management is more cohesive now. It is much more aggressive. It is getting the attention of the Secretary and the Deputy Secretary.

I have been to Chief of Mission conferences where drugs never came up before. That is not the case now, however. Things are changing. At each Chief of Mission conference, when the ambassadors of the region get together, now they talk about drugs and drug control. But that was not the case before.

Even in the past six months that has changed.

So the priority is there. But whether the results are there is too early to tell.

Mr. **Lewis**. Thank you.

Thank you, Mr. Chairman.

INM PROCUREMENT OF AVIATION PARTS

Mr. **Mrazek**. In your audit on the Narcotics Bureau procurement of aviation spare parts, you talked about the number of aircraft involved.

I will quote from the report. You say, "Taking advantage of the alternative procurement sources discussed in this report could save

INM at least one-third of its Fiscal Year 1990 aviation support costs, estimated at $64 million."

So that would be a saving in the neighborhood of $20 million.

Is the department moving forward with the recommendations that you made?

Mr. **Funk**. Yes, sir.

The $20 million is figured in this way. If we were to adopt a strategy of buying spares from Defense, getting some spares for free, which we can do, excess to Defense needs, particularly in the Huey choppers, that is now in line. That was not the case before.

We found almost a total ignoring of the resources available through Defense, either in depot maintenance, or in spares, or in cannibalizing the choppers. But that has changed.

If all these aggressive things are adopted, if we start buying on a competitive basis, if we start policing our procurements, and if we use all the resources of DOD, including those at Tucson and their depot maintenance in Oklahoma City, I believe that yes, money will be saved.

IMPACT OF NARCOTICS CONTROL PROGRAMS

Mr. **Mrazek**. I would just go back to one point again, and I do not mean to beat the proverbial dead horse. But I know that when Admiral Yost, the Commandant of the Coast Guard, came before our Subcommittee on Transportation asking for tens of millions of dollars in additional interdiction funds for the Coast Guard on top of hundreds of millions of dollars that the Coast Guard is presently using to interdict drugs, principally cocaine coming from the Caribbean, I asked Admiral Yost what percentage of the cocaine he felt was being interdicted as a result of those efforts, actually confiscated. His best assessment was a little less than 3 percent.

To the extent that we have to rely on your efforts as auditors of these programs and their effectiveness, I guess I am wondering how far you can go in examining programs that are just not getting the job done, and saying that this program isn't going to work.

Mr. **Funk**. Well, I have to say that our job——

Mr. **Mrazek**. Can you say that this policy isn't working and it's not going to work, and that you can spend more money or you can follow through on some of these recommendations.

Maybe you wouldn't say this in certain cases. But are you really precluded from saying that it is in your judgment——

Mr. **Funk**. Oh, certainly, certainly. I am not precluded at all.

We don't set policy. It is not my job as an IG to set policy. But we certainly can question.

In fact, by law, I am required to assess the conduct of diplomacy. That is one of the requirements in my law. And we do that. We go back to the Secretary and the Deputy Secretary regularly with things that we think are weaknesses.

These are not publicized. Obviously they are internal. We don't try to question these things in the open world. But we do so very aggressively.

You are raising such a difficult problem. Has there been improvement? Yes.

Admiral Yost says it is 3 percent. Last year it was 2 percent. So we have increased the interdiction by 1 percent.

Mr. **Mrazek**. I should say that he said last year a little less than 3 percent. But he said this year he was criticized so much for making that estimate that he was not going to make an estimate this year.

Mr. **Funk**. And, of course, we are dealing with situations around the world where the local police are grossly underpaid by our standards and where corruption, therefore, is an ever-present problem, in Southeast Asia as well as it is in South America.

Another difficulty is the profits are so great, if we choke off the growth of coca, it is liable to spring up—and, in fact, there are signs that it is springing up—in other countries. So all we are doing is squeezing one corner of the pillow and the other pops out.

That is a difficulty.

I have to say that we are doing a better job now than we were doing a year ago. Is that going to lead to success? It remains to be proven, sir.

Mr. **Mrazek**. So, 100 percent success, in terms of improvement, would be increasing the percentage of coca crops eradicated from 1 percent, based on your current estimate, to 2 percent?

Mr. **Funk**. No, sir. That would be playing games.

Mr. **Mrazek**. I agree.

Mr. **Funk**. At the same time the coca is increasing in production also. So we are fighting an uphill battle.

If we eliminate 1 percent and it increases 4 percent, are we then 3 percent ahead?

Mr. **Mrazek**. Thank you very much.

A.I.D. CONTRACEPTIVE PROGRAM

Before I turn to Mr. Lewis for questioning, I would ask General Beckington this question.

You referred on page five in your statement to having identified serious problems in the mode of delivery of contraceptive devices between 1982 and 1988.

There is a statement that A.I.D. procured $244 million of contraceptive devices, and that the audit of the procurement and distribution of these contraceptives found the program to be seriously flawed. That is the extent of your coverage of that.

Can you amplify a little on that program and on what the problem was?

General **Beckington**. That was, and remains, one of the centrally funded and centrally directed programs that I identified as having problems. We found in the course of that audit procurement problems, problems of estimating requirements. Remember, this program is one that is carried out in many countries. I forget the exact number. But it is somewhere in the neighborhood of 30 or 40 different countries.

We found shipping problems. We found inventory problems, both on the U.S. and the in-country end. We found distribution problems.

We also found quality control problems in the manufacture of these contraceptives, which were largely condoms. And we found accounting problems with respect to this program over losses, disposals of unusable commodities and problems with claims for lost and diverted commodities.

So it was kind of a range of problems across the entire program over a period of years.

Mr. **Mrazek**. It sounds like it.

General **Beckington**. The program, of course, is a very central one to the agency.

Mr. **Mrazek**. Did it take six years to find these problems? I ask only because you mentioned that in 1982 to 1988, we spent $244 million. From the standpoint of auditing these concerns, did they all just crop up at once? Or is it that there was just so much money going out that this program was not audited until a certain number of years after its inception.

General **Beckington**. It's the latter, really. It has to do with the whole problem of audit coverage, our ability to cover the agency's programs. This is one that we had not looked at. Until we finally did, the period of program life that we chose to look at was about a six year period. When we took this look, we found what we reported we found.

Mr. **Mrazek**. Has A.I.D. responded to those?

General **Beckington**. Yes. A.I.D. very definitely has responded in this instance.

Mr. **Mrazek**. Thank you.

Jerry, do you have any questions?

COOPERATION BETWEEN STATE AND A.I.D.

Mr. **Lewis**. Yes, thank you, Mr. Chairman. I have a couple of questions.

I suppose the initial question would be best addressed to Mr. Beckington of A.I.D., as well as Mr. Funk of State, although all of you probably should be communicating with one another about this question.

In testimony, Mr. Beckington, you mentioned the need for greater cooperation between State and A.I.D. It is a recommendation that has been around for a long, long time. And yet, there has been relatively little progress.

I would be interested in your opinions as to why the difficulty of effective cooperation continues to exist between State and A.I.D. I would be interested in your specific recommendations as to how we can improve that condition, maybe recommendations that you have not made before.

The ones that you have made before you can just put into the record.

General **Beckington**. I think your question, sir, is really directed to Mr. Funk. He was the one who made the comment about State and A.I.D. cooperation in respect, I think, to narcotics programs.

Mr. **Lewis**. Well, I frankly addressed it to both of you.

General **Beckington**. All right, sir.

Mr. **Funk**. Let me say this, Mr. Lewis.

If State and A.I.D. spoke as frequently and as candidly and as openly to each other as General Beckington and I do, I don't think there would be a problem.

But the fact is that there is a gulf—there should not be, but there is a gulf. As a result, we do not get in, up front, on the planning.

For example, our ambassadors have a good working knowledge of what the problems are, the economic problems in the various areas. It has always puzzled me why we don't get more into the upfront planning.

Sometimes there is a kind of dispirited answer. They say that the bloody grants are earmarked by the Hill, anyway, so what good is our doing any planning. And there is some truth in that, sir, because when you have that level of earmarking, it is rather difficult to persuade people to go in and plan.

But the fact is that the information that the mission directors of A.I.D. have and the information that the embassies have should be put together. We should be able to think more on a regional basis than we do. We should be thinking of development programs in East Africa, West Africa, or Central Africa, rather than country-by-country. The reason we don't do that partially is because the ambassadors are bilaterally oriented and not regionally oriented; it's partially because there is a jealousy and some friction here.

But that friction is usually in Washington. It is not in the field.

I know of very few cases where the mission director of A.I.D. is in a contest of any kind with the ambassador or the deputy chief of mission. This very rarely happens. The fights are up here, or the lack of conversation is up here. The lack of coordination is up here.

How can it be solved? By repeated banging away at the doors and saying we darn well have to talk together.

That is why I made the comment.

Mr. LEWIS. Aren't you two up here?

Mr. FUNK. Yes, sir. Pardon?

Mr. LEWIS. You two are up here, right?

Mr. FUNK. Yes, sir.

Let me tell you about the difficulty that is involved.

I was speaking to an ambassador in one of the key countries where drugs are located. He told me that many, many years ago, he was in the Peace Corps as a volunteer. He used to walk four days up to the capital city because there were no decent roads. This was years and years ago. He then noticed burro after burro with coca strapped to the animal.

He recently took a walk of two days along the same trail.

Mr. LEWIS. That was a substitute for hay, of course.

Mr. FUNK. I'm sorry?

Mr. LEWIS. It was a substitute for hay.

Mr. FUNK. A substitute for hay, yes, sir.

He took a walk along the same trail today and he did not pass any burro loaded with hay or coca. The reason was A.I.D. had put in a big infrastructure improvement. They built roads. So now the growers are pushing the stuff out on roads. They are not riding burros; they are riding trucks.

This is kind of the spinoff that you get sometimes. That can never be stopped.

But the point is if we talk together more closely, if, in fact, we were to coordinate as agencies more closely in doing planning, we would tie the infrastructure into the economic development system and also alternative crops. But this cannot be done separately. A.I.D. has the money; we don't have the money.

General BECKINGTON. Mr. Lewis, I don't really think that I am equipped to respond to your question. I have had no real reason to look closely at the subject of State-A.I.D. cooperation in any area of the agency's operations.

I do know that the policy decisions with respect to the ESF appropriation are ultimately made by the Secretary of State and not by my agency. There is back and forth in discussion, I am sure. But I simply am not personally knowledgeable about this particular issue, and I think it would be dangerous of me to attempt to comment in these circumstances.

Mr. LEWIS. You might at least let somebody know that we are asking these questions, so that there might be something put into the record on this.

Mr. FUNK. Let me read something, Mr. Lewis. In one of our reports, we recommended precisely that kind of tighter cooperation.

Assistant Secretary Levitsky came back, and I quote: "INM has approved U.S. A.I.D. regarding efforts to increase coordination of narcotics-related development"—in this case in Pakistan. "The cooperation is bearing fruit, and our cooperation should increase in the near future with the assignment to INM of an A.I.D. liaison officer who has extensive experience in Asia."

"One of this office's principal tasks will be to insure cooperation and coordination of a full range of projects—public awareness, income replacement, development assistance, technical support, and evaluation."

If, in fact, this happens, we will find out. This is the promise. We will have to look to see if it becomes an actuality.

AUDITING MAJOR AID PROGRAMS

Mr. LEWIS [presiding]. Unfortunately, we are going to have to recess for we have a vote. I am not going to be able to come back here because of the bill that is on the floor.

I want to ask several of you if you might respond, once we do come back, or at least for the record, and maybe for public discussion as well, to this. I specifically mentioned this item to Mr. Trodden.

I am interested in your highlighting special problems that you see that exist relative to auditing as they relate to those countries with whom we have major assistance relationships. The major three are Pakistan, Israel and Egypt.

I have had serious doubts myself about capital flows to Egypt in terms of those monies ever getting down to where people are. In this subject area, if there are special problems, I would like to have the committee know about them.

[The information follows:]

Mr. TRODDEN. Since the question refers to capital flows to foreign countries in monetary terms, I have referred this question to General Beckington for a response.

General BECKINGTON. The problems are not special Mr. Lewis. They are those associated with the same kind of issues outlined in my opening statement. If they sometimes seem special it may be because the A.I.D. flows to a country like Egypt are so large.

Mr. **Lewis**. We will recess now for a few moments.

[A brief recess was taken.]

RECURRING PERFORMANCE PROBLEMS IN A.I.D.

Mr. **Mrazek** [presiding]. I will call the hearing back to order and hope you will forgive the delay, gentlemen. It was caused by two consecutive votes on the floor.

General Beckington, one of the things that disturbed me a bit about your testimony was you said if we spend a day reviewing the last four or five semi-annual reports that you have sent to Congress and the GAO reports of the same period, we would be struck by the frequency with which the same problems emerged from the reporting.

I suppose one interpretation of that could mean that the program and management improvements are not being made in response to the Inspector General's reports and the GAO's reports. Is that the case?

General **Beckington**. Yes, I think it is, Mr. Chairman.

Mr. **Mrazek**. Why is that lack of responsiveness there?

General **Beckington**. I'm not sure that I am the best qualified to answer that.

The problems are there. I think that there are differing reasons for the agency's seeming inability to deal with them in an effective fashion.

On the host country contracting use, for example, I think if you were to ask the agency, you would find, among other things, that they say their staffing allowances are insufficient to permit the more heavy use of direct A.I.D. contract procedures.

On local currency issues, I think there is perhaps an honest disagreement with my view, as the Inspector General.

Whether there is or not I think, however, it should not delay some sort of reasonable solution to what actually is a problem.

We do not use local currency effectively, as I said in my statement. As a result, the impact, overall impact, of our economic foreign aid program is diluted, I think.

We had an example in Egypt about a year or so ago, a year and a half ago. It was—and I am speaking about these figures from memory—somewhere in the neighborhood of 750 million Egyptian pounds, supposedly, that was available to us, which accrued as a result, primarily, of the CIP program in that country.

At that time, that was the rough equivalent of about $350 million to $400 million U.S. dollars.

What was done with those currencies supposedly—and I really don't know because I have no way to audit them—is that they were turned over to the Ministry of Finance of the Government of Egypt, under an agreement by which the Ministry of Finance was to make these funds available to six different ministries of the Egyptian Government that were seen as having a development element in their mission, plus the ministry of supply.

From that point on, I certainly don't know what happened to them. I don't think the A.I.D. mission in Cairo knows precisely what happened to those funds, or the parent bureau here in Washington.

Now, I don't believe that is a good and effective way to use that kind of resource. That is where I have my problem and that is the kind of problem, although not the only kind of problem, that crops up regularly in my reviews of local currency situations. You will find them in the GAO's reports on the same types of issues.

Mr. **Mrazek**. What should we have done in that particular case?

General **Beckington**. I really don't know that I should try to answer that question so much, Mr. Chairman, as perhaps to say to you that I think the fundamental issue with respect to local currency is control and that we should find a way, "we," the Congress and the Executive Branch, to gain control of that local currency, so that the ultimate disposition and use of it, obviously in cooperation and coordination with the host country, but the ultimate decision-making authority with respect to that resource should rest with us, and it is not a matter of mutual agreement.

Mr. **Mrazek**. Well, it would seem to me that we certainly would have the leverage to do that.

General **Beckington**. I would think we would, too. Yes, sir.

SUSPENSION OF GUATEMALAN HEALTH PROGRAM

Mr. **Mrazek**. Thank you for that recommendation.

On a slightly different type of problem, I understand that very recently, this month, A.I.D. suspended a program in Guatemala, a $16 million program in Guatemala for immunization and anti-dehydration, because of some fraudulent actions and embezzlement by some Guatemalans involved in the program.

It is my understanding that the Guatemalan Health Minister has now charged that the people involved in the corruption were hired by A.I.D. I am wondering if you have any further details.

I have very sketchy information on this.

General **Beckington**. No, I do not at the moment, Mr. Chairman.

As a matter of fact, I was unaware until just now that the Minister of Health in Guatemala had made that sort of allegation or accusation.

I am aware of the suspension of the program. I am aware of the reason for the suspension of the program. It was the result of audit and investigative work carried out over the last several months by my regional office in Central America. The evidence adduced was sufficient so that the A.I.D. mission to Guatemala two weeks ago today, or tomorrow, as I recall, felt it necessary to suspend further disbursements with respect to that particular program. My memory is it was approximately a $16 million or so project.

Mr. **Mrazek**. Yes.

I have a report dated March 27, that the Guatemalan Health Minister publicly challenged U.S. Embassy Adviser John Treacy to prove that the people involved in the embezzlement of funds work in his ministry. It goes on through a variety of accusations and counter-accusations.

A.I.D. CORRUPTION CASES

Is this problem uncommon in Third World countries, where we run these kinds of immunization programs?

General Beckington. The fundamental problem of corruption is not uncommon in my experience and in my judgment, Mr. Chairman. It is one of the program environmental factors that makes it so difficult many times for the agency to conduct its business efficiently and effectively. It is one of the fundamental reasons why accountability should be a major focus, in my judgment, of my agency.

This takes time, this takes effort, this takes resources, and this takes an Inspector General. But, above all, it takes management alertness. In my experience, all too frequently we do not have that management alertness within my agency.

Mr. Mrazek. With respect to a number of A.I.D. employees who have been involved in corruption, those cases have come to light through auditing. There was one employee in Washington using travel vouchers who embezzled over $1 million. Another pleaded guilty for accepting bribes in the assistance program for the Contras.

If we did more aggressive auditing, would we find that there are more endemic problems with people who are not paid a great deal but who are monitoring a great deal of money and have access to a great deal of money?

Would we find a lot more problems like this, or is it really a rarity when it comes to corruption by A.I.D. employees?

General Beckington. I don't think I should even speculate on an answer to that question, Mr. Chairman. I just do not know what the answer might be.

I am struck by the frequency recently, within the last couple of years, of problems of this nature. But whether it is a trend, or whether it is a little spike of some kind, I really don't know.

I am startled because our selection processes are, I believe, very careful in determining the people that we recruit. They are well educated. They have clear records. They have to have a security clearance at a minimum of a Top Secret level, which means that they are not unknown quantities to us when we employ them.

So, I am surprised that we have had the number of problems recently that we have had. Whether we will see anything like it in the near-term or the mid-term, I really have no idea.

Mr. Mrazek. I would request, if possible, that you provide the committee a listing of actions against A.I.D. employees and A.I.D. contractors, and a brief description of each case over the last five years or so.

The subcommittee is aware, based on newspaper accounts, of over 50 employees involved in things, and it might be helpful to know whether there is an increase and what is the reason for that.

General Beckington. The comment I just made, Mr. Chairman, if I may interject, had to do with agency employees, not contractors or contractor employees.

Mr. Mrazek. Okay. But I would like to see that included as well, if possible.

Thank you, General.

General Beckington. Yes, sir.

[The information follows:]

AGENCY FOR INTERNATIONAL DEVELOPMENT
WASHINGTON, D.C. 20523

THE INSPECTOR GENERAL

April 24, 1990

The Honorable David R. Obey
Chairman, Committee on Appropriations
Subcommittee on Foreign Operations
House of Representatives
Washington, DC 20515

Dear Mr. Chairman:

During the course of my testimony before your Subcommittee on March 29, 1990, on the subject "Misuse of Foreign Aid" I was asked to provide a listing of actions against A.I.D. employees and contractors flowing from investigations of alleged misconduct. Data was requested for the past five years.

The data requested is contained in the attachments to this letter. It is sufficiently voluminous that I have chosen to forward it separately rather than try to insert it into the transcript of my March 29 testimony.

Sincerely,

Herbert L. Beckington

Attachments: a/s

A.I.D. OFFICE OF INVESTIGATIONS

INVESTIGATIVE STATISTICS

1985 - 1990

The A.I.D. Office of Investigations (IG/I) records were reviewed for the period January 1, 1985 through March 30, 1989 to determine how many investigations resulted in judicial or administrative action against the subjects of IG/I investigations. Below is a breakdown by eight (8) different categories:

Category I. United States Direct-Hire Employees: Judicial or administrative action was taken against 40 employees (both Foreign Service and Civil Service) for a variety of crimes and administrative irregularities.*

Category II. United States Personal Services Contractors (PSC): Administrative action was taken in 9 investigations of PSCs. No judicial action resulted.

Category III. Foreign Service National Direct Hire, Personal Service Contractors and Third Country Nationals: Judicial or administrative action was taken against 164 employees in this category.**

Category IV. Contractor Companies and Contractor Company Employees: In this category, judicial or administrative action was taken against 31 contractor companies and against 24 contractor company employees.

Category V. Suppliers and Commodity Import Program (CIP) Importers: Judicial or administrative action was taken against 32 suppliers and CIP importers.

Category VI. Grantees and Grantee Employees: In this category, judicial or administrative action was taken against 36 organizations and/or their employees.

Category VII. Private Voluntary Organizations (PVO) and PVO Employees: Judicial or administrative action was taken against 46 PVOs and/or their employees.

Category VIII. Host Government Project Personnel: Judicial or administrative action was taken against 67 host government project personnel.

In summary, judicial or administrative action was taken against 449 individuals and organizations involved in A.I.D. projects and programs worldwide over the past five years.

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* Brief descriptions of these cases are in Appendix A. Due to Privacy Act considerations, the names of the individuals are omitted.

** Brief Descriptions of a representative sampling of cases in this category are in Appendix B.

APPENDIX A

CATEGORY I: U.S. DIRECT HIRE EMPLOYEES

1985 - 1990

- Subject, a certifying officer in the financial management office, embezzled $1.2 million from A.I.D. He pled guilty to three felony counts and was sentenced to five years in prison and restitution of the embezzled funds.
- Employee admitted receipt of illegal payments from A.I.D. contractor and other improper activities during his implementation of a $90 million Malaria Research Project. Employee sentenced to three years' imprisonment, all but eight months of which were suspended and was fined $25,000.
- Employee pled guilty to misuse of diplomatic passport in gold, jewelry and currency smuggling operation. Sentenced to six months in jail, fined $15,000 and forfeited currency and jewels valued at $40,000. Resigned from A.I.D.
- Senior employee was found guilty of three counts of conflict of interest in hiring his wife as an A.I.D. contractor. He was sentenced to two years' probation on each count and fined $15,000.
- Employee indicted for defrauding U.S. Government by using evacuation funds to pay for son's visit from school to overseas mission. Trial pending.
- Employee pled guilty to two counts of bribery, admitting he accepted $93,000 from an A.I.D. contractor in return for releasing inside information to contractor. Sentencing pending.
- Employee was convicted on six counts of mail fraud and eight counts of embezzlement in connection with a illegal money exchange scheme while working as a budget and fiscal officer. He was sentenced to five years' imprisonment, all but six months of which were suspended. His employment was also terminated.
- Retired employee pled guilty to one count of mail fraud with regard to submission of false travel and allowance claims while assigned to an overseas office. He was sentenced to one year in prison and ordered to make restitution of $11,415.
- Civil suit filed against a former employee who had pled guilty to bribery and tax evasion in 1983 resulted in a civil judgment. Employee repaid $102,927 in back taxes, penalties and interest.
- Two employees went on a golf trip paid for by a contractor. One employee received a 60 day suspension without pay. The other was allowed to retire but his personnel file annotated to reflect he retired while under investigation for misconduct.

- Employee admitted being a co-conspirator with another A.I.D. employee in a gold/currency smuggling scheme. He retired in lieu of adverse administrative action.

- Three employees received free lunches at an exclusive club paid for by an A.I.D. contractor. Two employees retired and the third's personnel award was withheld. The latter individual also received a verbal reprimand.

- While working as a payroll clerk, an employee manipulated her pay records to obtain an overpayment of $265. She was sentenced to one year in prison, which was suspended. She also received one year's probation, was ordered to perform 50 hours' community service, make restitution and pay a $25 fine.

- Employee submitted false/misleading documents in connection with the importation of a tax free automobile which exceeded the cost limitation imposed by the U.S. Embassy. He was ordered removed from post by the Ambassador, given a reprimand and issued a bill for collection for $3,439.

- Employee sold his used computer to one of the overseas A.I.D. projects for $2,850 without informing the Mission Director. Since this action violated A.I.D. regulations, the sale was cancelled and the employee was reprimanded.

- Employee submitted a voucher for reimbursement of $2,200 for household furnishings. Investigation disclosed the actual cost of items was $699. Claim denied.

- Employee submitted false/misleading documents in connection with the importation of a tax free automobile which exceeded the cost limitation imposed by the U.S. Embassy. He was ordered removed from post by the Ambassador and was given a reprimand.

- Employee received a Separate Maintenance Allowance (SMA) in violation of A.I.D. regulations after he and his spouse had initiated divorce proceedings. Bill for collection for $2,871 issued.

- Employee was alleged to have paid $30 gratuity to a moving firm employee to under-report his household shipment's weight. He repaid $3,436 for excess weight charges.

- Senior employee had a close personnel friendship with a contractor employee who was fired for contract irregularities. Employee was orally reprimanded for not maintaining an arm's length relationship.

- Employee received a $13,500 educational allowance grant for her daughter but did not submit justification for the use of the grant funds. Inquiry disclosed she used almost half of the funds for other purposes. Bill for collection for $6,445 was issued to the employee.

- Employee altered her time cards after they had been reviewed and approved by her supervisor, thereby falsely claiming $2,898. She pled guilty to fraudulently receiving wages. She received a suspended sentence and agreed to make full restitution. She also resigned.

- Employee circumvented U.S. Embassy regulations which limited the amount of foreign currency he could exchange upon transfer from a foreign post. He was issued an oral admonition and his promotion to the Senior Foreign Service was withheld for one year.

- Employee accepted meals and cocktails from an A.I.D. contractor valued at $600. He was suspended without pay for ten days.

- Senior employee was involved in misuse of his official telephone, using his office to influence contract awards and other administrative irregularities. He received a reprimand and resigned from A.I.D.

- Employee received a free lunch from an A.I.D. contractor for which she received a verbal reprimand.

- Employee submitted a false hotel receipt with a travel voucher. He was suspended without pay for five days and directed to make restitution in the amount of $1,157.

- Employee cashed several Non Sufficient Fund (NSF) checks to an Embassy cashier's office. Full restitution was made ($350) and letter of reprimand was issued to the employee.

- After severely damaging his motor vehicle in an accident, employee received authorization to replace his vehicle. He repaired the vehicle which he claimed was unrepairable and then claimed $1,242.65 for freight and clearance costs for a second car he had imported a year prior to date of accident. Employee refunded full amount received for the second car.

- Employee misused a U.S. Government vehicle. He repaid $418.30 after being issued a of Bill for Collection.

- Employee accepted free air fare valued in excess of $2,000 for his wife and himself from the airline. He was suspended for ten days without pay.

- Retired senior employee repaid $3,275 for personal calls made from his official telephone.

- Employee tried to force an A.I.D. contractor to sell him a project vehicle. He received a letter of reprimand.

- Employee, who served as a timekeeper, pleaded guilty to falsifying her time cards and obtaining $1,600 illegally. She received one year probation and was ordered to make full restitution. Employee resigned in lieu of dismissal.

- Employee received letter of admonition for entering into an agreement with a private institution which provided him with $10,000 to support his research project in return for ownership of book he intended to write. At the time, he was in training status with A.I.D.

- Senior employee charged approximately $9,751 in personal telephone calls and other personal expenses to A.I.D. Charges recovered by deductions from employee's retirement annuity payments.

- Employee instructed subordinates to violate U.S. Government regulations by allowing him to pay cash for an airline ticket for an official trip in lieu of using a Government Transportation Request so he could obtain a free round trip ticket for his wife from travel agent. He received a thirty day suspension without pay.

APPENDIX B

CATEGORY III: SELECTED CASES INVOLVING
FOREIGN SERVICE NATIONAL EMPLOYEES*
1985 - 1990

- A procurement specialist collected over $250,000 in bribes from A.I.D. suppliers over 2 1/2 year period. His job was terminated. He was sentenced in U.S. Federal District Court to two years imprisonment, all but six months of which were suspended. He also received a $25,000 fine.

- An Assistant Project Officer was convicted of embezzling about $10,000 from a USAID-funded project. He had received the money to purchase 10,380 jute bags but used the funds for personal expenditures. The court ordered he repay the project and suspended his one-year sentence. He had served two years in prison during the various judicial proceedings.

- Employee embezzled almost $4,000 from A.I.D. over a year period. He was arrested and sentenced to a year in prison and fined. The court ordered restitution.

- Two employees' jobs were terminated after it was discovered one of them, a project officer, had approved vouchers supported by false invoices, forged receipts and previously paid invoices from a company which was 90% owned by his wife. The second employee was involved with the project officer. Wife's company was debarred from doing business with A.I.D.

- Employee was paid by A.I.D. contractors to act as a clearing agent and expeditor. His employment was terminated.

- Employee claimed $1,545 in illegitimate costs on his travel voucher. Employee's job was terminated and his last two pay checks were applied toward the loss.

- Employee recommended host country procurement be made from a company in which he was an officer. His employment was terminated.

- Three employees made 46 unauthorized overseas telephone calls using a direct dial telephone line located at the USAID Mission. They were required to make restitution and their employment was terminated.

- A senior employee was dismissed after he violated standard contract procedures by conducting an unauthorized evaluation of price quotations and unilaterally awarding a contract.

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* All incidents in this category occurred at overseas A.I.D. Missions.

- An employee managing a $500,000 per year Participant Training Program selected three of her brothers for long-term academic training in the U.S. at a cost of $247,756. She also created false documentation to justify a $70,000 grant to her sister. She was fired and $134,000 was reprogrammed after her sister's scholarship was revoked and a brother was recalled from the U.S. where he was in training.
- A conspiracy among an A.I.D. project accountant, a bank teller and two businessmen resulted in the loss of several thousand dollars to a USAID Mission. After checks were signed by an A.I.D. official, the amounts of the checks were inflated and the checks were cashed by the accountant. All three individuals were arrested and the accountant repaid the money. He also lost his job on the A.I.D. project.
- A warehouseman attempted to sell a bag of computer parts belonging to a USAID Mission. The parts, valued between $1,600 to $2,300, would not fit any computers in the host country except the USAID's. The parts were recovered and the employee was dismissed.

AUDITING PROBLEMS WITH FMS COMMERCIAL CONTRACTING

Mr. **Mrazek**. With respect to FMS cases that you had spoken about, Mr. Trodden, we have had over the last ten years a remarkable number of foreign military corruption cases. In each case, it would appear that the problem has been found not because the defense contractor, the auditing agency, the DOD Inspector General, or the GAO auditor found anything wrong, but because something went wrong with the product or else someone told about the bribery or the kickbacks.

Do you agree that the FMS corruption cases virtually all seem to occur in the commercial contracting area, where the U.S. is asked to pay for a contract negotiated between a foreign government and an American contractor?

Mr. **Trodden**. Mr. Chairman, as a general proposition, I believe that to be correct.

I need to have a little bit of a bureaucratic disclaimer here in that I'm on the audit side of the house, and the investigative side, the Defense Criminal Investigative Service, and so forth, has been involved in some of those criminal cases that you talk about.

As a general proposition, I do believe, however, that your statement is correct, that the investigation, in the first place, did not arise out of pro-active audit work that we had done as much as it did out of deficiencies in the product, or whistle blowers, or things of that nature.

Mr. **Mrazek**. Mr. Conahan, do you have a viewpoint on that?

Mr. **Conahan**. Yes, and I would agree with Mr. Trodden.

Program audit, for the most part, will not uncover the kind of wrong-doing that you are referring to. Most of that comes about as a result of hot lines that are set up by Inspectors General, or ourselves, for that matter, from tips, from whistle blowers, from disgruntled people, both within the government as well as in contractor operations.

Mr. **Mrazek**. Do you think that it would be useful to go back to what Congress used to do in terms of these contracts and that is to require that all grant funded foreign military contracts go through the DOD procurement process, rather than through these commercial contracting approaches?

Mr. **Conahan**. I would like to defer the answer on that question until we complete a body of work that we plan to begin very soon in connection, primarily, with the Israeli program, and also build on the larger body of work that Mr. Trodden has underway right now, that will be completed sometime this spring, I believe.

Mr. **Trodden**. Correct.

Mr. **Mrazek**. With respect to the more than 800 commercial FMS contracts that are written each year, is this body of work that you are talking about, is this the first, real, significant auditing that has been done of the commercial contracting procedures?

Mr. **Conahan**. Being handled through the foreign military sales program, yes, sir.

You see, what happened is that we had a big shift here. We had primarily a grant aid program early-on; then we had primarily a foreign military sales program, until earlier in this decade, when we begin seeing increases in grant aid.

Then, we had a change in the legislation which allows the grant aid program to be carried out under the Arms Export Control Act. So this is relatively new.

Mr. **Mrazek**. When are those reports to be concluded?

Mr. **Conahan**. Well, our work is just beginning this month. I will defer to Mr. Trodden on his.

Mr. **Trodden**. Mr. Chairman, I am advised that our draft report should be finished in June of this year, which would put the final report in roughly the August timeframe.

CAMBODIAN A.I.D. PROGRAM

Mr. **Mrazek**. Thank you.

With respect to covert programs, we are obviously aware of the major problem in Thailand, in which Thai military officers appeared to be siphoning off a substantial portion of the covert assistance that we were attempting to provide for the non-Khmer Rouge resistance in Cambodia. The press has also reported on corruption problems with Pakistani officers, who were stealing money that we had in the pipeline for the Afghan resistance.

I am wondering whether you have comments on what you believe could be done, or should be done, in order to insure adequate controls on covert programs, or programs that are handled in a quiet manner, and are delivered to areas where there is no American presence?

General **Beckington**. That question may be addressed to me, Mr. Chairman. I think these are A.I.D. programs that you may have in mind.

Mr. **Mrazek**. Okay. Yes, that is true.

General **Beckington**. Well, in the first instance, Mr. Chairman, my recommendation would be that A.I.D. not be entrusted with a program of this nature.

The rules, the laws, and the regulations under which we operate—and here I am speaking specifically to rules dealing with accountability, control, and integrity, program integrity—make it very, very difficult for my agency to handle such a program.

I think there are other elements of the government that are better equipped, better staffed, and better trained to handle this type of program. The Cambodian program is an overt program in the sense that everyone knows it exists; but its methods of operation are covert. Because of that latter condition, we ran into severe difficulties in the integrity of the program.

They have been now, I think, as fully addressed as they can be under AID's regulations, and the way we addressed them, the way the agency addressed them, was essentially to take over almost total control of the procurement and the movement within Thailand of the commodities involved, which placed a heavier stress on my agency.

Mr. **Mrazek**. I have seen press accounts that suggest that American equipment was sold openly in Thailand. I am curious as to whether we investigate things like that.

General **Beckington**. We did investigate up to a point, Mr. Chairman. Beyond that point, I was not allowed to investigate, and I reported those circumstances to the Congress at the time.

Mr. **Mrazek**. Not allowed by the Thai Government?

General **Beckington**. By our government.

Mr. **Mrazek**. Why would we not want to see something like that fully investigated, if equipment that was supposed to go to the non-communist resistance ended up being sold in Thailand on the open market? Why wouldn't that be something worth looking into?

General **Beckington**. Mr. Chairman, I am getting very uncomfortable. I am more than ready to answer your questions, but I do not think I should do so in open session.

Mr. **Mrazek**. I see. Okay. I appreciate that.

AUDITING THE ACQUISITION OF MILITARY GOODS

Back to you, Mr. Trodden.

We got testimony through the GAO that the Salvadoran Air Force sold $1.6 million worth of fuel, originally bought and purchased with U.S. military grant funds, sold it back to the U.S. Government, and to the Contra supply operation. In June of last year, Congress was assured in Department of Defense testimony that the DOD had taken appropriate steps to insure that payments received for authorized transfers are properly controlled and reutilized.

This testimony is apparently untrue because the subcommittee is informed that funds were used by the Salvadoran military to make over $1 million in commercial purchases, including $350,000 for a building, a car, and other personal items for a Salvadoran military officer here in Washington, and for other things.

In terms of the overall problem, with respect to other countries that receive fuel from the U.S., like El Salvador, are there steps that can be taken to see whether these abuses are occurring in other programs? Have they been audited? Are there new guidelines being initiated to avoid this problem in the future?

Mr. **Trodden**. I will stipulate at the front end of this answer, Mr. Chairman, that there is a visibility problem from our standpoint, when we audit, or attempt to audit, the acquisition of military goods by some of the countries to whom we sell.

Basically, our audit work has been in the acquisition arena: good pricing; is the source of supply in fact domestic; and so forth.

Once title transfers to the customer, our ability to get behind that, as to what subsequently happens to the hardware, for example, is very, very difficult.

I mentioned in my statement that we are currently engaged in an audit of the Stinger missile, and I think some of the answers to your question may arise from that. We will be attempting to trace deliveries of all Stinger missiles produced to the various sources to which they had been sent.

There is an open question in my mind as to the access that we are going to have, the visibility, the receptivity of some of those countries to the trafficking in those missiles. I think that is an open question.

SEPARATE ACCOUNTS FOR AID FUNDS

Mr. **Mrazek**. This next question is a kind of A.I.D./GAO question, if you will. Unless my colleagues on the subcommittee have further questions, I think we will probably conclude after these next questions.

Several years ago, at Congressman Lehman's suggestion, Congress passed legislation which required that economic support funds, dollars and local currencies, for El Salvador be placed in separate accounts in the central bank in order to help prevent corruption problems, and later that legislation was expanded to include all cash transfer ESF assistance.

Then, in the 1990 bill, Congress required that the separate accounts requirement also be applied to nonproject sector assistance. Both A.I.D. and GAO testimony state that the separate accounts have been helpful, but that problems still continue in this area.

I am wondering if you could expand on your comments concerning local currency and cash transfer problems.

For example, should PL480 funds also be brought under this legislation?

Mr. CONAHAN. We found that, for the most parts, these separate accounts indeed have been set up for the cash transfers.

There are two big problems that remain. Number one, A.I.D. does not have procedures to verify if, indeed, what is reported by the recipient governments is, indeed, the case. The procedures do not exist and, therefore, there is no way of really validating or verifying that that is the case.

Secondly, there is no standard, indeed, for auditing by anyone who would be involved in the audit. We're talking about whether it would be the A.I.D. auditors, whether it be CPA firms, whether it be local accounting firms and the recipient governments, or, indeed, the supreme audit institution of the recipient.

So there are two rather substantial problems as far as we are concerned.

Now, when it comes to local currency, whether we need a special account for local currency, it seems to me that that issue can be debated. I think that the notion of a special account is not as important as somehow or other trying to get a handle on the attitude of the agency with respect to not only local currency but control in general.

A.I.D. ATTITUDINAL PROBLEM

You asked a question earlier and I would like to take this opportunity to comment on it because I think it is apropos.

Why do these conditions continue to exist despite the many recommendations made by the Inspector General, by the General Accounting Office?

I think that there is a fundamental management philosophy in the Agency for International Development that goes to getting projects approved, to obligating funds up front; to make sure that the dollars that are made available get committed.

There is very little time left over by A.I.D. officers to tend to the implementation of their activities, to the monitoring of those activities.

Somehow or other we have to build up a reward system over there that goes to monitoring and managing, as well as committing funds. This has been a long-time problem, and I would maybe like for General Beckington to comment on it as well.

So I think the issue of whether we have a separate account or not can be debated. I am not going to come down one way or the other on that at the moment.

But the other issue I think is really terribly important, and we have to get to it somehow.

Mr. MRAZEK. General Beckington?

General BECKINGTON. Yes, I would associate myself with the remarks you have just heard and the answer you have just been given. There is an attitudinal problem, I think. The agency is not as concerned about accountability and holding people to performance, and by "people" here I am not speaking necessarily within the agency so much as I am our relationships with the countries where we are delivering foreign aid.

We find repeatedly that conditionality associated with foreign aid projects are not enforced by my agency. We find repeatedly the host country contribution problem. We find repeatedly the confusion and disarray in the local currency accounts.

These are problems that are discernible, they are identifiable, they are measurable in most cases, and they should be the kind that we, as smart managers, should be able to deal with.

People can disagree on what the solution might be, but there is nothing unusual about that. It should be worked out, a decision made, and we should all march to the same drummer and in the same direction with regard to that solution.

On the specific point that started your question, the special accounts that really originated in this subcommittee, the agency has not yet put into place fully the procedures necessary to insure that we know what the Congress tells us we have to know, which is that we must be able to track those dollars from the point of transfer to the point of end use. We do not yet have in place, after some three or four years' experience, a system that will always assure us of that. And I don't think we have yet come to grips with the most recent legislation that you mentioned, the sector cash transfer issue.

I believe that we should move out smartly on both of those.

Mr. MRAZEK. Were you also associating yourself with Mr. Conahan's comments with respect to this being an attitudinal problem? Is that the primary concern—attitude?

If it is attitude, one would think that the Administrator would be in a position to enforce new guidelines. If it is a matter of lack of staffing, simply because of budgetary constraints to really do the follow-through, that would be another problem.

Is it a combination?

General BECKINGTON. I think it is a combination. Yes, sir. I think there is some attitudinal aspect to the problem. I think that there is merit to the agency's concerns that they are understaffed and under-resourced, if you will, given the nature and the environment of the foreign aid program.

As I said at the outset of my testimony, economic foreign aid is a tough job to do. I do not really know of one that is much tougher in the Federal Government. And a smart organization under those circumstances organizes and equips itself to operate in the environment that it knows it's going to have to operate in. We have not been able as an agency, I do not believe—and I am speaking now as an observer, but a close observer—we have not been able to do that as well and as fully as we might, particularly in recent years.

Mr. **Mrazek**. Would you have recommendations, Mr. Conahan, as far as solving the attitudinal aspect of the problem?

Mr. **Conahan**. I think, as you suggested, Mr. Chairman, it has to start at the top. I think that the Administrator has to enunciate a policy which says that accountability and control is as important to this agency as is getting the money under contract, as it is in getting projects committed, and that sort of thing.

Then I think you have to have a reward system, an appraisal system, that takes that into account; that, indeed, as people are rated, as people are appraised on the kind of job they are doing, that their supervisors look very closely at the kinds of jobs they have done in their respective areas with respect to getting the kind of accountability and control that is needed over whatever their respective activity is.

It has to be ingrained in the entire management philosophy and appraisal process of the agency.

Mr. **Mrazek**. Well, we're going to develop report language which will accompany our bill this year stressing exactly that. I am sure the Administrator of A.I.D. will take those words to heart.

The hearing has been very helpful to me, very constructive in terms of learning a lot more about a subject that I wasn't as informed about as I should be, perhaps. I am confident that all of the other members of the subcommittee who were not here will diligently read your testimony when they curl up in bed tonight.

[General laughter.]

Mr. **Mrazek**. I do want to thank you very much for coming. I appreciate it very much.

This hearing is now adjourned.

Questions for the Record From Mr. Obey

SUBMITTED TO STATE DEPARTMENT INSPECTOR/GENERAL

ECONOMIC AND BUSINESS AFFAIRS BUREAU

Question. Mr. Funk, your office has also issued a report on the Bureau of Economic and Business Affairs at the State Department. While that bureau is not directly funded by this subcommittee, I was interested in that report because we do fund the Export-Import Bank, the Trade and Development Program, and the Mixed Credits Program in the economic support fund.

The U.S. trade deficit is a continuing major economic problem for our economy—it was over $105 billion last year—you would think that the administration would be well organized and coordinated in trying to address that problem, but we have not seen any clear economic strategy being developed to address the trade deficit—other than the devaluation of the dollar which took place several years ago.

Would you briefly summarize the problems that you found at the Economic and Business Affairs Bureau and what the Department is doing to respond to your recommendations?

Answer. The inspection of the Economic and Business Affairs Bureau (EB) of the Department of State was conducted in July-August 1989, and the report was published in January 1990.

Generally, the report has a critical tone, and it reflects the major theme that, while the morale and performance of the EB Bureau are very good in many respects, its overall effectiveness is being significantly hampered by external and internal management factors which, to some extent, are beyond the Bureau's control.

The major findings and recommendations of the inspection report were the following:

The Bureau of Economic and Business Affairs is a talented, but troubled Bureau that seeks to serve the Secretary of State assertively, but it suffers from a perceived decline of influence and prestige among competing Bureaus within the Department, and among outside Agencies, due to the shifting over the past decade of the prime responsibility for the determination of U.S. international economic policies from State to other, so-called "lead" Agencies in Washington.

Some of the "lead" Agencies have established by legislation, such as the U.S. Trade Representative (USTR) in the trade field, and the Department of Commerce in export promotion; others have resulted from executive decision, such as the lead role of the Treasury Department concerning the debt problems of developing countries.

The overall result of these developments has been an observable sense of loss of Department of State predominance in important areas of economic policy, such as export promotion, trade negotiations, international investment, and commodity issues. This, in turn, has engendered problems of self-doubt and declining self-esteem among many career economic officers of the Department assigned to the EB Bureau.

Other contributing factors to the decline of EB's influence and standing within the Washington economic community have included inadequate access to top-level policy guidance, and a reputation within EB for a management style which, while activist and policy focused, has appeared too frequently to be uncoordinated and non-collegial.

Needed changes in EB operations include: (1) a more open, clear, and consultative EB management style; (2) improved management procedures (especially better internal communications focusing on policy guidance, coordination, and feedback); (3) fuller and more coordinated economic policy guidance of feedback from Department principals; (4) better synthesis in meshing the policy needs of the Secretary with the operations of EB; (5) better collaboration with other Bureaus, Agencies, and the Congress; and (6) a unifying and viable concept of EB policy goals and objectives.

The Department of State also needs to clarify the economic policy functions of the Department, and the professional future of its career economic officers. At the same time, EB officers need to be more stalwart in seeking guidance, in expressing professional judgments, and in recognizing that knowledge and skill are as important as formal mandates in determining policy.

Moral within EB needs to improved. The strength of EB is the high quality of its personnel who are generally respected both inside and outside the Department for their competence. However, along with major initiatives to enhance their impact on policy decisions, programs also are needed to develop a proactive training system (including management training), and effective orientation program, space adjustments, and improvements in shabby office conditions within EB.

The EB structure also should be revised to remove anomalies, avoid duplication, and gain potential savings both in positions and funding. Some ten positions within EB were recommended variously for changes in function, or for reprogramming to meet new requirements for expanded support to business and commercial activities, and to meet growing responsibilities related to controls over technology transfers to other countries.

Since EB'S success is heavily dependent upon technical expertise in various areas, assignments of Foreign Service Officers to EB should be longer than the standard two-year tours which are customary within the Department; otherwise, greater reliance by EB on Civil Service economists will be necessary.

Management controls within EB generally are adequate, but the Bureau needs to ensure that all its officers are alert to their responsiblities for appropriate controls for avoiding waste, fraud, abuse or mismanagement.

Generally speaking, the reaction of senior State management to the inspection report on the EB Bureau has been very positive. Both Secretary Baker and Deputy Secretary Eagleburger have emphasized in recent public statements their personal concern for the continuation of a strong role for the Department of State in the economic policy field, and the high priority which they assign to the economic function at our foreign Service posts abroad. Within the EB Bureau itself, Assistant Secretary McAllister and his senior officers are moving to implement the great majority of the recommendations made in the inspection report.

We foresee some improvement in EB Bureau operations as the result of these responses to our inspection recommendations. However, the major issue remains one that is difficult to grapple with in the short term—the changing role and influence of the Department of State in international economic policy formulation. This is a subject which doubtless will continue to occupy the attention of both the White House and the Congress, as we move to deal with the evolving international economic problems and opportunities of the 1990's.

SUBMITTED TO A.I.D. INSPECTOR GENERAL

SEPARATE ACCOUNTS REQUIREMENTS

Question. Several years ago, at Congressman Lehman's suggestion, the Congress passed legislation which required that economic support fund dollars and local currencies for El Salvador be placed in separate accounts in the central bank in order to help prevent corruption problems.

Later, that legislation was broadened to include all cash transfer ESF assistance.

Then, in the FY 1990 bill, Congress required that the separate accounts requirement also be applied to non-project sector assistance.

Should P.L. 480 funds also be brought under this legislation?

Answer. Mr. Chairman, accountability of local currency accruing from any A.I.D. program, including P.L. 480, is strengthened by the use of special accounts.

FOREIGN EXCHANGE AUCTIONS AND MONETARY UNIONS

Question. Open foreign exchange auctions, and monetary unions which some African countries belong to represent fairly unique situations for the separate accounts requirements. Should exemptions be granted for these situations, or do you believe that preventing commingling of foreign exchange dollars is more important than free and open foreign exchange systems? Why?

Answer. Mr. Chairman, in our review of ESF dollar cash transfers used to conduct foreign exchange auctions, accountability for the U.S. dollars through monitoring the deposit and disbursement transaction through the separate accounts appears to be in compliance with the legal requirements applicable to cash transfers.

Local currency received by the auction of U.S. funds are placed in separate accounts and jointly programmed in accordance with procedures established between A.I.D. and the host country in the cash transfer agreement. I do not believe that in this type of situation the exemption issue need arise.

In those countries where there are Monetary Unions, tracking of dollars past the point where the currency conversion takes place is not possible. The CFA is a common currency used in West African countries that is backed by the French Franc. The CFA is the currency actually transferred into separate accounts of the host countries in the African Monetary Union for carrying out A.I.D. assistance. This is the point at which the use of the assistance should be monitored by A.I.D. to ensure that the agreed upon development purposes are accomplished. Again, I do not believe the exemption issue need arise with respect to the dollars. However, the local curency separate account must be monitored closely.

HOST COUNTRY CONTRACTING

Question. Both the A.I.D./IG and the GAO have found that host country contracting—where A.I.D. is the source of funding, but where they are not party to the contract, which is negotiated by the country and the contractor—presents special problems that are not being adequately addressed by A.I.D.

Should A.I.D. insist on direct contracts in certain countries which have bad histories?

Answer. Mr. Chairman, I believe so. The Agency's experience with the use of the host country contracting procedure has been a troubled one as attested to by both my reports and those of the GAO. The Agency needs to be much more disciplined and selective in employing this type of contracting in the LDC environment.

Question. Should A.I.D. have contract and procurement training for host country officials?

Answer. Mr. Chairman, I believe there will be frequent instances where this type of training can contribute to development. This is also true of financial managment and public administration. A.I.D.'s Bureau for Latin America and the Caribbean has been giving increased attention recently to training in financial management, for example.

Question. What actions could A.I.D. take across the board to improve performance in this area?

Answer. A.I.D. should adhere to its own procedures which require a careful assessment of the host country's capability before reaching a determination to use the hose country contracting approach. Frequently we find this important step has not been taken; at other times the review has been inadequately thorough. Once underway host country contracts should be monitored. One of the hazards of the host country mode is a tendency on the part of A.I.D. to stand aloof once contract performance gets underway. Performance problems are not detected as they develop, corrective action is slow to take place and is often awkward because A.I.D. is not one of the contracting parties. Finally, countries that are clearly experiencing difficulties under the host country system should not employ it. The contracting mode used—host country or A.I.D. direct, should be the one promising the most effective and efficient delivery of the aid.

MICROENTERPRISE PROGRAM

Question. The group RESULTS came out with a study in November critical of A.I.D. for not, in their view, implementing the FY 1988 microenterprise appropriation earmark in accordance with congressional report recommendations. The chief congressional report recommendations were that 80% of the loans under this program be targeted at the poorest 20% of the population and that loan size not exceed $300 unless circumstances require a large size to accomplish objectives of the program. RESULTS found that of $31.8 million reported for ten countries comprising half of the microenterprise earmark, only $5.2 million was spent in ways that would fulfill or approach congressional intent. In addition to programmatic and policy questions, their findings raise a number of questions regarding A.I.D. management.

In trying to obtain data on A.I.D. FY 1988 microenterprise expenditures in ten countries, RESULTS found that A.I.D. would report different figures at different times. For example, in a March 30, 1989 letter to Congress, A.I.D. reported $7.97 million for Indonesia, but in a September 1989 cable from A.I.D./Indonesia only $2.19 million was reported.

What are we to make of the confusion over A.I.D. figures on microenterprise?

Is the IG Office looking at the management systems which led to the conflicting data provided on microenterprise?

Does the larger number of small microenterprise loans administered through Private Voluntary Organizations (PVOs), Non-Governmental Organizations (NGOs), and banks lend itself to abuse?

Is A.I.D. capable of monitoring all these loans?

Answer. Mr. Chairman, I am not in a position to respond to your specific questions on the Microenterprise Program. It is a relatively new program for A.I.D. and we have as yet done no audit work with respect to it.

On your general question, the vulnerability of the program to abuse, it is my view that it is very much the type of program which can lend itself to abuse unless it is tautly managed.

A.I.D. is probably going to have difficulty monitoring such a program—great difficulty, primarily because it is management intensive and A.I.D. is already thinly spread.

MISUSE OF ECONOMIC ASSISTANCE FUNDS

Question. Please put the issue of abuse of funds into perspective. For instance, what proportion of economic assistance in an average year raised questions of abuse?

Answer. Mr. Chairman, I have no sound basis for answering this question. Our audit coverage of the total foreign aid program is limited and quite selective even with the added IG staffing provided by the Congress over the past three years.

Question. To your knowledge, has there ever been an effort to quantify abuse across the Government? If so, how does A.I.D. compare to other government departments and agencies?

Answer. Mr. Chairman, I know of no effort to quantify abuse across the Government. I am of the opinion, as you know, that A.I.D. by the nature of its mission is highly vulnerable to abuse.

Question. From your experience can you identify any particular sector and type of project which are most liable to abuse, which are most liable to mismanagement, and which are liable not to be implemented according to plan?

Answer. Mr. Chairman, any type of project employing host country contracting, requiring cost sharing or host country contributions and dependent upon host country financial management, local currency accountability and cash management is at risk of mismanagement by both A.I.D. and the host country. Problems in these areas are stubborn and have been proven resistant to correction for years.

Question. Do you think there is a problem in general with the process in which A.I.D. develops and designs projects?

Answer. Mr. Chairman, we do find problems in project design, on a case-by-case basis. However, I believe that more significant problems exist in implementing, evaluating and managing projects. A great deal of time is spent on designing ideal projects and not enough effort is spent on implementing. Consequently, projects often fall behind schedule, fall short of planned results or in some cases simply fail.

Question. Some A.I.D. project officers suggest that greater funding should be made available for operational costs so that missions can explore project feasibility more thoroughly before committing to the long process of project design and agreement. Would a larger pool of project development money contribute to better designed and more appropriate projects?

Answer. Mr. Chairman, in theory, if thoughtfully done, more money and time on project planning and development should lead to more successful developmental projects and contribute more towards our economic development objectives. A potential pitfall here, however, is the pressure exerted on planning by the yearly obligation cycle.

Question. The Inspector General (IG) report criticizes the Swaziland primary health care project's design for including "overly ambitious targets which were neither specific nor measurable." To what extent, in your view, is this the case with other A.I.D. projects?

Answer. Mr. Chairman: We do find, with considerable frequency, that project designers often establish overly ambitious and complex goals and often do not adequately quantify or measure progress and results being achieved or missed. This is a part of the implementation problem noted earlier.

Question. A frequent criticism found in IG reports is that the *host country contribution* is not forthcoming as agreed in the project document. In your estimate, to what degree is this the case worldwide in a given year?

Answer. I believe that the failure of host governments to adhere to agreed cost sharing is a broad based problem in A.I.D. We often find projects where outputs have to be reduced, or where projects are not sustained after A.I.D. funding ends because host governments fail to provide their agreed upon financial support. The system used to obtain host country reimbursement is not working effectively.

I believe A.I.D. should consider establishing payment procedures similar to those our domestic agencies employ in administering cost sharing or matching programs. Each party to the agreement contributes their share or percentage of costs as the costs are incurred. Then, quarterly expenditure reports reconcile each party's contribution to ensure agreed upon contributions are made. This process works well in our domestic programs.

In A.I.D., the reimbursement process does not work this way. Too often A.I.D. contributes its share according to the agreement while host governments or PVOs do not. We often find that the non-A.I.D. share never materializes for various reasons. The particular project is scaled back, outputs reduced or in some cases the project merely ceases or fails. If both parties contributed their agreed share as the project progresses—this would not happen. Both parties would be committed to ensuring the projects success and continued viability after the U.S. funding ceases. I believe this cost sharing problem has to be addressed and cured if we want to attain the objectives of cost sharing.

Question. Should the host contribution language in the agreements be more strictly designed to insure the contribution is made? How might this be accomplished?

Answer. As stated in the previous answer, a quarterly reconciliation with contributions from both parties as costs are incurred is my recommended approach. Our domestic agencies have found this approach to be successful.

Question. A.I.D. is responsible for allocating funds to several agencies, including the Department of Energy and the Environmental Protection Agency, which are implementing aspects of the Support for East European Democracy Act of 1989 (SEED). What kind of control is A.I.D. exercising to insure that funds it allocates to these other agencies are not misused? Will the A.I.D. IG Office audit the activities of these agencies in this regard?

Answer. The funds authorized by the Congress in the Support for East European Democracy Act of 1989 (SEED) are appropriated to A.I.D. and therefore, I consider A.I.D. to be responsible and accountable for these funds. We are currently working with agency managers to embed into the grant agreements requirements for record keeping, access to these records and annual audits. My office will either make audits of these grants or review the quality of audits made by other parties such as CPA firms under contract. I do believe that audits of the SEED funds are essential to good accountability.

A.I.D. CONTRACTOR CONFLICT OF INTEREST

Question. Several industry sources have brought to the committee's attention potential conflict of interest situations with A.I.D. support contractors.

In several cases allegedly A.I.D. support contractors working in Indonesia in the energy area attempted to manipulate the project process in order to enrich their companies.

Allegedly, A.I.D. support contractors would mutually advise A.I.D. Mission Directors against proceeding on a specific project. The same A.I.D. support contractors would then contact prospective contractors and offer to change their recommendation to A.I.D. in exchange for involvement in the prospective contract. There are allegations of this type of thing occurring on at least three occasions. Apparently, there have been similar problems in the Department of Energy with support contractors.

Do you know anything about these allegations?

Answer. Mr. Chairman, I am not familiar with these allegations. Perhaps the Subcommittee staff could provide me with additional information if it is available.

Question. Does A.I.D. have sufficient guidelines to protect against this type of activity?

Answer. I think A.I.D. has adequate guidelines to prevent this type of misconduct, but no guidelines can fully protect against deliberate malfeasance.

SUBMITTED TO DEPARTMENT OF DEFENSE INSPECTOR GENERAL

BROAD BASED REVIEW OF SECURITY ASSISTANCE

Question. Mr. Trodden, your testimony focuses on a new broad based inspections of the security assistance programs.

This committee has been frustrated for many years with the FMS accounting procedures, the FMS Trust Fund, FMS corruption cases, the lack of adequate FMS commercial contract oversight and any number of other problems. Would you tell us more about your findings and what changes you are recommending?

Answer. Mr. Chairman, our audit work on commercial sales financed with FMS credits is currently being finalized. While it is too early to state what our recommendations will be, the audit has focused on the approval process controlled by the Defense Security Assistance Agency. Tentatively, we believe that more effort needs to be expended on those procurements that are made without the benefit of adequate competition. We believe that the Defense Security Assistance Agency can do more in the way of price and cost analysis on those procurements. However, we are not sure that the Defense Security Assistance Agency has the proper staffing needed to properly control these procurements. This is a frustrating area. We would like to believe that the recipient countries are just as interested or as competent as we are on maximizing the use of these funds. Unfortunately, that does not seem to be the case across the board. Seemingly, some countries do a better job than others in protecting these resources. Consequently, it is difficult in establishing a fixed set of rules to govern by. And the use of variable sets of rules may be politically unsound.

Question. Your testimony mentions the need to expand the oversight of direct commercial sales. Would you expand on the problems that you found that led to that recommendation?

Answer. Mr. Chairman, I wouldn't say that the need to expand the oversight of direct commercial sales necessarily stemmed from any particular problems. We are of course concerned about overcharges and the product substitution cases that have been identified by the Defense Criminal Investigative Service. But, we also looked at the trends in the Security Assistance Program. I believe that a lot of the reported problems in the Foreign Military Sales Program are being cleaned up. We are finding that DoD is not subsidizing foreign military sales like it was in the past. In fact, we are finding instances where the foreign customers are being overcharged. We also recognize that the FMS financing program is becoming larger with the transfer of the Military Assistance Program to FMS Financing. In FY 1991, we will establish a research program to look at the types of auditing we can and should be doing in the FMS Financing Program. This research will address such issues as pricing, competition, foreign offsets, quality assurance, etc.

Question. You also talk about correcting the FMS accounting system. People have been talking about and working on that for years with little success. Where do those efforts stand, and when do you think we might have a new system in place?

Answer. I believe that the accounting problems that have been identified in the Foreign Military Sales Program are coming under control. In 1982, we recommended that a new FMS trust fund be established to control new FMS cases. We made this recommendation because the existing trust fund was out of balance and could not be balanced. FMS disbursements were recorded at country level, while FMS performance was recorded at the case level. Out case level records were out of balance with the country level records at one time by more than $1 billion. With impetus from the Congress, changes have been made in the FMS accounting system. In 1989, DoD began recording cash disbursements at the case level. This improvement represents a major milestone in FMS accounting. It will now be possible to reconcile cash and performance at the case level rather than at the country level. The Security Assistance Accounting Center has also established cash transactions controls that will insure that all reported cash transactions are recorded. We have recommended that this control be extended to delivery reporting. We plan to start an audit of disbursement reporting this summer to see if these controls are working and whether appropriate actions are being taken to correct past disbursements that were reported without country or case identity. The Air Force Audit Agency is also doing some work in this area and should have a report available early this summary. GAO has also made some positive comments on the accounting changes that are taking place.

SALE OF MILITARY FUELS

Question. GAO testimony indicates that the Salvadoran Air Force sold $1.6 million in fuel, originally bought with U.S. Military Grant Funds, back to the U.S. Government, its contractors, and to the illegal contra supply operation.

Further, Congress was assured in DoD testimony in a June 1989 hearing that: "DoD had taken appropriate steps to ensure that payments received for authorized transfers are properly controlled and reutilized."

This testimony apparently was untrue. Funds were used by the Salvadoran Military to make over $1 million in commercial purchases including $350,000 for a building, a car for a Salvadoran military officer in Washington, and for other purposes.

Mr. Trodden, what other countries receive fuel from the U.S. like El Salvador, and have any steps been taken to see whether or not abuses are occurring in those programs?

Answer. Mr. Chairman, the Defense Security Assistance Agency has informed me that in addition to El Salvador, Honduras, Israel and the Philippines have also received fuel under our assistance programs. Since 1982, El Salvador has been the largest recipient of grant aid fuel ($26.3 million). Israel was second at $13.6 million; Honduras was third at $12.0 million; and the Philippines was last at $5.4 million.

Question. Have they been audited?

Answer. We have not performed any audits of these fuel transfers. In 1989, we did some audit work in Honduras. As a part of that effort, we looked at the Military Assistance that was being provided to Honduras. While controls were in place that provided an audit trail as to what material had been transferred, there were no apparent finite controls over the materiel after it had been transferred.

Question. Has DoD initiated any new guidelines on fuel sales that you know of?

Answer. Mr. Chairman, in February of this year, the Under Secretary of Defense for Policy sent a message to the overseas security assistance offices that expressed concern over the accounting problems that resulted from commingling FMS and non FMS-origin consumable items, including bulk petroleum. This message read in part, "Special care must be taken to ensure that minor repair parts, fuel, or other defense articles which lose identity when commingled, are controlled by the recipient government using a procedure which will reasonably assure there will be no non-approved transfers. . . . For the first three years following delivery of an item purchased with U.S. security assistance funds, the Defense Security Assistance Agency will normally concur with transfer only where the proceeds of the sale are deposited in the country's Trust Fund account". I believe that these added controls will be difficult to enforce. We could probably stop the generation of funds on the resale of fuels to the U.S. Government by establishing procedures to replace the product in kind rather than providing cash payment. I don't how difficult this would be to administer and it would not provide control over third party transfers.

FMS CORRUPTION CASES

Question. During the past ten years, we have had a remarkable number of foreign military corruption cases.

The Justice Department has investigated and prosecuted cases concerning abuses in the Philippines, El Salvador, Niger, Egypt, and South Korean programs, and other investigations continue.

We have also had rewrites of the foreign military procurement guidelines both in 1984, and again last year in order to help prosecute these problems.

In each case, I believe that the problem has been found not because the Defense Contract Audit Agency (DCAA) or the DoD Inspector General or the GAO audited and found any thing wrong, but because something went wrong with the product when someone tried to use it, or someone told about the bribery or kickbacks.

The Government of Israel was allowed to set up a military purchasing office in New York to handle its large volume of FMS purchasing. Would you tell us about the size and activities of this office? Have any audits of any of its activities been undertaken by any entity of the U.S. Government to your knowledge?

Answer. According to the Defense Security Assistance Agency, the Israeli buying office as about 250 people. According to the information we obtained during our current audit, the buying office uses slightly over $1 billion a year of FMS credits to finance direct commercial sales. Other than our audit work in 1983, I have no knowledge of any other audit work undertaken by any entity of the U.S. Government. As previously stated, the GAO has just announced new work in this area.

Question. In the 1989 Appropriations Bill, which we passed on October 1, 1988, the Congress required that: "That the Department of Defense shall conduct during the current fiscal year nonreimbursable audits of private firms whose contracts are made directly with foreign governments and are financed with funds made available under this heading (as well as subcontractors there under) as requested by the Defense Security Assistance Agency."

Can you tell the Committee what audits were requested by DSAA to be done, and regardless of a DSAA request, what audits were done by the Defense Contract Audit Agency? (I think you will find that the legislation has been ignored)

Answer. As I stated in my testimony, we were unaware of the new language in the appropriations act until I was recently approached by the new Comptroller of the Defense Security Assistance Agency. The Defense Contract Audit Agency has agreed to do the audits that will be requested by DSAA.

The Defense Security Assistance Agency provided us with copies of six audit reports issued by DCAA since October 28, 1987. These reports primarily involve a determination of origin of the materials being provided under the selected contracts. As you are probably aware, FMS credits can only be used to finance materiel of U.S. origin.

CONTROL OF CORRUPTION IN COVERT PROGRAMS

Question. The press has reported corruption problems with Pakistani officers stealing assistance that was intended for the Afghan rebels. The program in Thailand that provides assistance to the Cambodian resistance forces has also been reported to have ripped off by Thai military officers.

What do you believe should be and can be done in order to ensure adequate controls on programs that are either covert or are handled in a quiet manner or are delivered to areas which have seen no American presence?

Answer. We don't have oversight over covert programs in the military assistance arena, which are managed by other than DoD agencies. In our current audit of the Stinger missile, we have identified a number of missiles that were transferred outside of the Department of Defense. Once we have determined that Defense was properly reimbursed for these missiles and have determined that Defense is no longer responsible for their safeguard and accountability, we will not perform any additional audit work. I believe the audit and inspection responsibility should lie with the agency that controls the convert programs.

TECHNOLOGY TRANSFERS

Question. The U.S. has coproduction facilities with a number of countries. There have been reported cases of transfers of coproduced items or other items for which we have given the technology ending up in some unusual places.

Would you tell the committee some background concerning the Korean M-16 Rifle program, the Israeli cluster bomb, about the export of chrome-plated connon barrels to Israel, and any other cases that you know about? How can this situation be better controlled?

Answer. I share your concerns on the transfer of technology. On November 7, 1985, we issued "Report on the Audit of the Sale of DoD-Owned Technology and Royalty Fee Recoupments for Foreign Military Sales Customers," (Report No. 86-037). This audit showed that the procedures for controlling the transfer of Government-owned technology to foreign military sales customers were inadequate. During the audit, we identified transfers of technical data packages that could be used to produce U.S. military equipment although the stated purposes of these transfers were only to enable the foreign countries to operate and maintain existing U.S. equipment or to study the feasibility of producing the material. We recommended that the issuance of technical data packages be discontinued for other than production purposes, and better controls be established over foreign production.

This report resulted in a number of changes to the controls over technical data packages. I would like to mention that during the audit, we did not identify any transfers of our "leading edge" technology.

If I recall correctly, we were not able to access the Korean production facility for the M-16 Rifle. Therefore, we could not determine whether the actual co-production quantities were accurately reported. The Security Assistance Management Manual provides for audit access to co-production facilities on a case-by-case basis. I would prefer that the audit access be extended to all co-production agreements.

I am not familiar with the Israeli cluster bomb and the export of chrome-plated cannon barrels to Israel. In this latter instance, export controls start with the Department of Commerce. DoD only becomes involved when the Department of Commerce forwards the request for export license to DoD for concurrence.

Question. Both Egyptian and Pakistani individuals have been arrested trying to steal American military technology. What other countries that we give foreign aid to have been caught trying to steal U.S. technology?

Answer. I am not aware of any other countries that we give foreign aid to being caught trying to steal U.S. technology.

Question. Considering the difficulties the United States has experienced with coproduction programs, should we restructure the system for approving and supervising agreements, or perhaps reconsider our basic policies?

Answer. Short of having full-time U.S. inspection personnel at the coproduction facility, I know of no way that we can be assured that the authorized production quantities are not exceeded. From a diplomatic standpoint, this may not be a practical solution. If we want to be absolutely certain the quantities are not exceeded, then the Congress may want to consider disallowing any future coproduction arrangements. However, any such action would have to be carefully weighed against its impact on international security. Also, this action would not preclude unauthorized production from technical data packages that have been previously released to foreign governments.

SUBMITTED TO GENERAL ACCOUNTING OFFICE

FMS CORRUPTION CASES

Question. During the past ten years we have had a remarkable number of foreign military corruption cases. The Justice Department has investigated and prosecuted cases concerning abuses in the Philippines, El Salvador, Niger, Egypt, and South Korean programs, and other investigations continue. We have also had rewrites of the foreign military procurement guidelines both in 1984, and again last year in order to help prosecute these problems. In each case, I believe that the problem has been found not because the Defense Contract Audit Agency (DCAA) or the DOD Inspector General or the GAO audited and found anything wrong, but because something went wrong with the product when somebody tried to use it, or someone told about the bribery or kickbacks. The Government of Israel was allowed to set up a military purchasing office in New York to handle its large volume of FMS purchasing. Would you tell us about the size and activities of this office? Have any audits of any of its activities been undertaken by any entity of the U.S. government to your knowledge?

Answer. According to Israeli officials, the Israeli Purchasing Mission's primary function is to procure items for the Israeli Defense Force. The Mission employs about 240 people located at the Mission in New York. Additional personnel are located at various U.S. military bases and contractor facilities.

GAO's ongoing review of U.S. controls over commercial military purchases by Israel funded by foreign military sales (FMS) credits will likely be our most detailed work to date involving the activities of the Mission. It follows our review entitled SECURITY ASSISTANCE: Reporting of Program Content Changes being done at your request. This latter review involved work at the Mission regarding its role in the reporting of changes in the Israeli military aid program. In addition to these current assignments, four other GAO assignments have included work at the Mission. These were FOREIGN ASSISTANCE: U.S. Funds Used for Terminating Israel's Lavi Aircraft Program (GAO/NSIAD-90-3, Oct. 26, 1989), ISRAEL: Use of U.S.-Manufactured Tear Gas in the Occupied Territories (GAO/NSIAD-89-117, Mar. 22, 1989), FOREIGN ASSISTANCE: Analysis of Cost Estimates for Israel's Lavi Aircraft (GAO/NSIAD-87-76, Jan. 31, 1987), and U.S. Assistance to the State of Israel (GAO/ID-83-5, May 27, 1983).

Question. In the 1989 Appropriations bill, which we passed October 1, 1988, the Congress required that: "the Department of Defense shall conduct during the current fiscal year nonreimbursable audits of private firms whose contracts are made directly with foreign governments and are financed with funds made available under this heading (as well as subcontractors there under) as requested by the Defense Security Assistance Agency." Can you tell the Committee what audits were requested by DSAA to be done, and regardless of a DSAA request, what audits were done by the Defense Contract Audit Agency?

Answer. According to DOD officials, in fiscal year 1989, DSAA did not request any audits of private firms whose contracts are made directly with foreign governments and are financed by the FMS program. For fiscal year 1990, DSAA recently provided DCAA with a memorandum on types of contracts for possible audit and guidelines of audit parameters. A meeting is scheduled for May 1990 to identify specific contracts to be audited.

CONTROL OF CORRUPTION IN COVERT PROGRAMS

Question. The press has reported corruption problems with Pakistani officers stealing assistance that was intended for the Afghan rebels. The program in Thailand that provided assistance to the Cambodian resistance forces has also been reported to have been ripped off by the Thai military. What do you believe should be and can be done in order to ensure adequate controls on programs that are either covert or are handled in a quiet manner or are delivered in areas which have no American presence?

Answer. We believe that the General Accounting Office needs to review these programs. Our basic audit authority is contained in the Budget and Accounting Act of 1921, the Accounting and Auditing Act of 1950, the Legislative Reorganization Act of 1970, the Congressional Budget and Impoundment Act of 1974, and the General Accounting Office At of 1980. As an independent, nonpolitical agency in the legislative branch of the federal government, GAO's authority is extensive, encompassing not only financial auditing, but also management reviews and evaluations of the effectiveness of programs. These statutes authorize GAO to audit the activities of executive branch agencies, and grant it access to the records of the agencies necessary to discharge this responsibility.

While there is an undisputed need to protect covert operations from risk of exposure, the Iran-Contra affair has demonstrated the risks that, in the absence of independent auditing, covert operations might deviate from policies established by the Congress.

GAO has been unable to conduct financial and program audits because of the CIA's refusal to grant GAO access to CIA documents and personnel. If GAO is expected to audit these programs, we need to have full and complete access to information to fulfill our audit requirements.

TECHNOLOGY TRANSFERS

Question. The U.S. has coproduction facilities with a number of countries. There have been reported cases of transfers of coproduced items or other items for which we have given the technology ending up in some unusual places. Would you tell the Committee some background concerning the Korean M-16 rifle program?

Answer. In the Korean M-16 rifle program, using U.S. financial and technical assistance, Korea built a plant capable of producing 100 percent of the M-16 rifle and its parts—a capability not matched in the United States or anywhere else in the world. A government-to-government Memorandum of Understanding and a commercial licensing and technical assistance agreement governed the quantities of rifles and spare parts authorized for production in Korea. These agreements further restricted third party transfers and sales of the rifles and parts, requiring prior U.S. government consent. We found that U.S. government oversight of the program became very limited once production of the rifle was fully underway, and Korea exceeded authorized production quantities and made unauthorized sales agreements with third parties. According to information available to us, in one of these cases a delivery was made. In addition, Colt Industries—the U.S. producer of the M-16 rifle—identified cases of unauthorized sales and deliveries of M-16 parts to Indonesia.

Question. How can this situation be better controlled?

Answer. In our report MILITARY COPRODUCTION: U.S. Management of Programs Worldwide (GAO/NSIAD-89-117, Mar. 22, 1989), we identified numerous cases in which items being produced under government-to-government Memorandums of Understanding and Letters of Offer and Acceptance were sold to third countries without the required U.S. government consent. In the cases we identified, the U.S. government would not have approved the sales directly from the United States, and, therefore, would not have approved a third party sale. We found that there were no direct controls or monitoring and that indirect controls were limited in these programs for ensuring that agreements restrictions on quantities authorized for production and third party sales were honored. We made a number of recommendations to improve the controls in and oversight of these programs. If properly implemented, actions we recommended in our report should improve controls over the unauthorized production and sale of U.S. coproduced weapons and items. Additional information is provided separately due to classification.

Question. Would you tell the Committee some background concerning the Israeli cluster bomb, about the export of chrome-plated cannon barrels to Israel, and any other cases that you know about? How can this situation be better controlled?

Answer. We do not have any information on these specific cases.

Question. Both Egyptian and Pakistani individuals have been arrested trying to steal American military technology, what other countries that we give foreign aid to have been caught trying to steal U.S. military technology?

Answer. We have provided this information separately due to classification.

SEPARATE ACCOUNTS REQUIREMENTS

Question. Several years ago, at Congressman Lehman's suggestion, the Congress passed legislation which required that Economic Support Fund dollars and local currencies for El Salvador be placed in separate accounts in the central bank in order to help prevent corruption problems. Later, that legislation was broadened to include all cash transfer ESF assistance. Then, in the 1990 bill, Congress required that the separate accounts requirement also be applied to non-project sector assistance. Should PL 480 funds also be brought under this legislation? Open Foreign exchange auctions, and monetary unions which some African countries belong to represent fairly unique situations for the separate accounts requirements. Should exemptions be granted for these situations, or do you believe that preventing commingling of foreign exchange dollars is more important than free and open foreign exchange systems?

Answer. While we have not specifically addressed the issue of separate accounts for P.L. 480-generated local currencies, we believe that separate accounts, whether for Economic Support Fund-generated local currency or for P.L. 480-generated local currency, strengthen AID's ability to assure that (1) agreed upon deposits are made and (2) funds are used for agreed upon purposes. There is, of course, much more that needs to be done to assure that proper control and accountability is maintained over local currencies generated through U.S. programs, and some of these actions have been suggested by AID's Office of Financial Management. These include, for example, (1) requiring formal and standard financial assessments of host country agencies using such lcoal currencies, (2) strengthening host country reporting requirements and AID mission verification procedures, and (3) requiring annual audits of host country agencies managing the local currency accounts and using the funds. With regard to maintaining separate foreign exchange accounts when foregin exchange auctions are used, we have reported [1] that it is unclear how AID would be able to avoid commingling cash transfer funds with other foreign exchange under these circumstances. In that report, we pointd out that the system of host country foreign exchange auctions helps to establish a fair market value for the country's currency and is an equitable means of allocating foreign exchange. In such cases, countries commingle U.S. cash transfers with other donor's contributions, thereby precluding a direct tracking of funds to their end use. Thus, it was unclear how the segregation of funds, as called for by AID guidance, could be accomplished.

With regard to cash transfers to countries belonging to monetary unions, we found that AID was working out an arrangement with the West Africa Monetary Union to provide a subaccounting for U.S. cash transfers deposited in the Union's pooled account. At the time we completed our review, AID had not issued guidance on how AID officials should handle cash transfers going into monetary union countries. Thus, in keeping with congressional intent that AID implement separate accounting, we recommended that AID describe how it could maintain accountability in cash transfer programs when it could not avoid commingling cash transfers with other foreign exchange. This recommendation was not to suggest that AID should forego its support of such programs, but we believe that AID should be able to explain in its cash transfer program documents why it cannot avoid commingling and the means through which it will maintain program accountability.

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[1] *FOREIGN AID: Improving the Impact and Control of Economic Support Funds* (GAO/NSIAD-88-182, June 29, 1988.)

Host Country Contracting

Question. Both the AID/IG and the GAO have found that host country contracting—where AID is the source of funding, but where they are not party to the contract, which is negotiated by the country and the contractor—presents special problems that are not being adequately addressed by AID. Should AID insist on direct contracts in certain countries which have bad histories?

Answer. AID has no formal stated preferences for either AID direct or host country contracts. This policy is a prudent one since it allows AID mission officials to decide on a case-by-case basis which contracting mode is more appropriate. This flexibility is necessary because such decisions can be influenced by a number of practical and political considerations which cannot be reduced to a set formula to determine when a host country contract should be used. Based on preliminary audit work, we believe that AID officials, as a general rule, attempt to strike a reasonable balance among the many considerations involved—one of which is the reputation of the host government and individual agencies responsible for contract administration.

Question. Should AID have contract and procurement training for host country officials?

Answer. No basis for comment. We have performed no detailed audit work on this issue.

Question. What actions could AID take across the board to improve performance in this area?

Answer. GAO's on-going review of AID's use of host country contracting will address a number of areas where AID can improve its oversight of host country contracts. Due for release in late 1990, our report will focus on deficiencies in AID's assessments of host agency contracting and voucher review capabilities; the need for improved oversight of the contract award process; the lack of proper audit coverage; and AID's failure to track and implement its own procedural and management safeguards, which were designed to limit AID vulnerability to fraud, waste, and abuse. These early findings will be developed at length in our final report, which will include specific recommendations on how AID can improve its oversight of host country contracts.

Microenterprise Program

Question. The group RESULTS came out with a study in November critical of AID for not, in their view, implementing the FY 1998 microenterprise appropriation earmark in accordance with congressional report recommendations. The chief congressional report recommendations were that 80% of the loans under this program be targeted at the poorest 20% of the population and that loan size not exceed $300 unless circumstances require a larger size to accomplish objectives of the program. RESULTS found that of $31.8 million reported for ten countries comprising half of the micro-enterprise earmark, only $5.2 million was spent in ways that would fulfill or approach congressional intent. In addition to programmatic and policy questions, their findings raise a number of questions regarding AID management.

At the request of Senator DeConcini and Representatives Feighan and Gilman, the GAO is conducting an investigation to determine AID compliance with the FY 1989 earmark on microenterprise. What is the status of that investigation? What issues regarding AID management have been raised by the investigation so far?

Answer. We have completed initial work at AID/Washington and will begin our field work at missions in Bangladesh, Senegal, Guatemala, and Jamaica in May. The requestors asked us to visit the Grameen Bank in Bangladesh, which is widely cited as an example of a successful small credit program for the poor. We chose to review the micro-enterprise programs in Senegal, Guatemala, and Jamaica because AID statistics show that these countries received about 28 percent of AID micro-enterprise loan funding in fiscal year 1989. We have agreed to testify at hearings tentatively scheduled for late June, and to issue a report later this year. Based on our work to date, we are pursuing the following issues.

How does AID manage the micro-enterprise program? According to AID Washington officials, the program is decentralized with its missions primarily implementing the program through intermediaries which, in turn, work directly with grassroots organizations in identifying micro-enterprise needs for credit assistance and the size of loans. We will also ascertain how the missions manage the micro-enterprise program and to what extent the missions work with the grassroots organizations in planning and implementing the program. We will obtain the views of mission officials on the feasibility of the committee reports' guidelines and discuss if they are better alternatives for assuring that micro-enterprises have access to credit.

How reliable is the data on micro-enterprise loans submitted to Congress by AID in its March 30, 1990 report? To prepare the report, in January 1990, AID asked its missions to provide certain information concerning their micro-enterprise programs. However, the reliability of the data has been questioned. Reportedly, the information submitted by the missions contains inconsistencies and is based on estimates of the average loan size and economic status and gender of the loan recipients. We will assess the methodology AID used to compile and analyze the data in AID's recent report.

Questions for the Record From Mr. Porter

SUBMITTED TO A.I.D. INSPECTOR GENERAL

FAMILY PLANNING PROGRAM

Question. Mr. Beckington, on page five of your statement you described that the distribution system for contraceptive devices was "seriously flawed."

It is my understanding that the IG has made seven specific recommendations concerning this program and that A.I.D.'s Population Office will begin implementation of all these recommendations by the end of March. Is that true?

Answer. Yes. The Agency moved swiftly to correct the problems found by our audit of the procurement and distribution of contraceptive devices. For example, the Agency has already intiated action to move to direct procurement to gain more control over that aspect of the program. Our audit follow-up and resolution procedures are closely following the action on the audit.

SUBMITTED TO DEPARTMENT OF DEFENSE INSEPCTOR GENERAL

ISRAELI MILITARY PURCHASES

Question. Mr. Trodden, on page 8 of your testimony, you noted that your own audit of the Israeli military buying office was terminated in favor of an ongoing GAO audit that was also terminated. In order to restore confidence that this program is going well, and I have heard of no allegations to the contrary, what progress have you made in getting either you or the GAO to monitor this program?

Answer. Mr. Congressman, on April 12, 1990, GAO announced that it was restarting its survey to examine the adequacy and implementation of U.S. controls over commercial military purchases by Israel financed with Foreign Military Sales Credits. GAO's primary objective is to determine whether U.S. monitoring and review of Israel's commercial military purchases are adequate to assure the propriety of the purchases and the payments.

SUBMITTED TO GENERAL ACCOUNTING OFFICE

AID PROGRAM IN LIBERIA

Question. Mr. Conahan, on page 6 of your prepared statement, you described problems with our aid program in Liberia. It is my understanding that AID took almost direct control on this program several years ago, including the requirement of AID cosignatories on many checks leaving the Liberian Treasury. Have those reforms failed and, given the worsening strife and human rights situation in Liberia, should we begin to wind down our program there?

Answer. In response to our report LIBERIA: Need to Improve Accountability and Control Over U.S. Assistance (GAO/NSIAD-87-173, July 16, 1987), AID stated that it would take a number of steps to strengthen controls over the U.S. assistance program in Liberia, including (1) providing a team of operational experts to work in key financial positions within the Liberian government to strengthen accountabilty and (2) designing additional controls over counterpart funds generated from P.L. 480 food assistance.

According to AID officials, the operational expert program, which began in early 1988 and included countersigning authority for the U.S. experts in a number of Liberian agencies, was terminated in November 1988. The program failed because the Liberian government lacked commitment to budgetary reforms and because it was unwilling to cooperate with the U.S. team in developing controls over significant revenue and expenditure sources. Program documents indicate that most of the Liberian agencies included in the program violated the terms of the program agreement.

AID officials indicated that the mission in Monrovia has taken a number of steps to strengthen controls over the P.L. 480 program, including (1) using private sector distributors to handle food imports, (2) using commercial banks to deposit counterpart funds generated from food sales, (3) requiring prior approval authority before disbursement from local currency accounts, and (4) installing an audit program for the special accounts. Problems continue, however, including Liberia's failure to pay its arrearages for food assistance loans. AID officials also noted that the Liberian government is again overdue in paying its arrearages on other U.S. loans. As required by U.S. legislation (Sec. 518 of the Foreign Operations, Export Financing, and Related Programs Appropriation Act, 1990), AID is in the process of phasing out development assistance programs in Liberia because of the country's failure to pay arrearages.

KOREAN RIFLE SALES

Question. Mr. Conahan, on page 15 of your statement you told us that the Koreans had violated their agreement with the U.S. by trying to sell M-16 rifles to unauthorized third parties. Who were those third parties?

Answer. We have provided this information separately due to classification.

AFGHANISTAN AID PROGRAM

Question. Mr. Conahan, on page 18, you described the totally uncooperative policy of the CIA in your attempts to audit the Afghan aid program. Have there been any later attempts by GAO to look at this program?

Answer. Our last attempt was in response to a July 1989 request by the Congressional Task Force on Afghanistan to review U.S. covert military aid to the Afghan resistance. In February 1990, we terminated our work because the CIA would not allow to us to review its role in the program.

FUEL PROVISION PROGRAMS

Question. Mr. Conahan, on page 21, you document many serious problems in the provision of fuel supplies to the El Salvadorans and then implicate other fuel provision programs in Honduras, Israel, and the Philippines. Do you have any substantive evidence of mismanagement in these other programs?

Answer. My remarks on page 21 were intended to point out what we view as a prudent management response for an agency to pursue upon learning that one of its programs had been compromised. Given the circumstances of the Salvador case, we do not believe that an DOD must have specific evidence of mismanagement in its other fuel assistance programs before chceking them for possible problems. These programs have similar operating characteristics as the Salvador program.

Subsequent to the hearing, DSAA personnel met with my staff to discuss drafting a cable tasking U.S. officials in Honduras, Israel, and the Philippines to review the respective fuel assistance programs. DSAA has prepared a draft cable; my staff has reviewed it; and it should be sent out shortly.

A.I.D.'S MONITORING AND REPORTING OF CONSULTING SERVICES

Mr. OBEY. At this point we will include in the record a letter from the Agency for International Development Inspector General on A.I.D.'s progress in complying with the requirements for monitoring and reporting consulting services.

[The information follows:]

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AGENCY FOR INTERNATIONAL DEVELOPMENT
WASHINGTON, D.C. 20523

THE INSPECTOR GENERAL

MA 2 1

The Honorable Jamie L. Whitten
Chairman, Committee on Appropriations
House of Representatives
Washington, D.C. 20515

Dear Mr. Chairman:

In accordance with Section 1114 (b) of the Money and Finance Enactment Act of 1982 (P.L. 97-258), we have completed our review of A.I.D.'s compliance with the requirements for monitoring and reporting consulting services. The Act requires Inspectors General to submit to the Congress an evaluation of agencies' progress in (1) instituting effective management controls over the use of consulting services, and (2) improving the accuracy and completeness of the consulting services contract information provided to the Federal Procurement Data System (FPDS).

A.I.D. established a system of management controls over the use and reporting of consulting services, and submitted the required financial information on such services to the FPDS. However, A.I.D. still needed to provide more definitive guidance to implement the new requirements stipulated under the latest Office of Management and Budget (OMB) guidelines. Namely, A.I.D. needed to designate a single official to be responsible for ensuring the proper use of consulting services; institute better management controls over the evaluation and reporting of consulting services; and improve documentation to support budget justification information submitted to the Congress.

Management Controls - The revised OMB Circular A-120, dated January 1988, provided new policy guidance on consulting services and required a series of specific controls for the management of such services. One requirement of the revised circular was the designation of a single official reporting directly to the head of the agency who will be responsible for ensuring the proper use of consulting services. A.I.D. had not designated a single responsible official as required. The responsibility for managing consulting services was being shared by several A.I.D. offices.

The Circular also required each Federal agency to evaluate the consulting services, at the conclusion of the contract arrangement, to assess its utility to the agency and the performance of the contractor. A.I.D. had not established the procedures to implement this requirement and had not performed the required evaluations. Responsible A.I.D. contracting officials stated that they would address these issues as part of their current efforts to revise A.I.D.'s internal guidelines in accordance with the latest OMB Circular.

Contract Reporting - In January 1988, OMB revised Circular A-120 expanding the definition of consulting services to include a wide range of advisory and assistance services, such as management and professional services, special studies, analyses, and evaluations. To implement this change, the Federal Acquisition Regulations were revised in November 1988. However, A.I.D. did not update its Acquisition Regulations (A.I.D. Handbook 14) to reflect the expanded definition. The existing A.I.D. Handbook, therefore, was outdated, and many A.I.D. contracting officers in the field were still classifying and reporting contracts according to the old definition.

This reporting resulted in understating A.I.D.'s use of consulting services in the reports submitted to the FPDS. In its report to the FPDS, for example, A.I.D. reported for fiscal year 1988, 92 consulting services contracts totaling $2.5 million. Based on a recent special review conducted by A.I.D. using the new expanded OMB definition, A.I.D. estimated the amount of consulting services used for that year would have been about $40 million if the new OMB definition had been in effect during that period. A.I.D. was unable to determine the level of consulting services used for the fiscal year 1989 because the appropriate change to the Federal Acquisition Regulations implementing the revised OMB definition of consulting services was not made until after the start of the fiscal year. As of February 1990, A.I.D. had initiated measures to amend its internal regulations to bring them into conformity with the current Federal Acquisition Regulations.

Budget Justifications - In February 1990, A.I.D. finalized a draft of its 1991 budget justifications on consulting services to be submitted to the Congress. At the time of this letter, the draft was being printed for formal publication. The draft included the financial estimates of proposed consulting services and related justifications. However, the consulting services data reported in the amount of $46.6 million were based on estimates and not supported by detailed documentation. A.I.D. officials stated that they had to use these estimates because of the revision and expansion of the definition of consulting services under the new OMB guidelines. They added that they were in the process of developing a new contract information management system which will include the necessary data elements on consulting services, and thus the consulting services information derived from this system and reported to the Congress in the future would be fully supported.

In summary, A.I.D. had generally complied with its requirements with Public Law 97-258 and OMB Circular A-120 governing the use and reporting of consulting services. However, A.I.D. still needed to provide better guidance and procedures to ensure that the contracting officials effectively adhere to the requirements stipulated under the new OMB guidelines with respect to the designation of a single responsible official, evaluation of consultants' performance, and classification of consulting services. The Agency also needed to improve documentation to support budget justification information to the Congress.

Sincerely,

H L Beckington

Herbert L. Beckington

TUESDAY, APRIL 3, 1990.

ENVIRONMENTAL ISSUES

WITNESS

HON. GAYLORD NELSON, WILDERNESS SOCIETY

CHAIRMAN'S OPENING STATEMENT

Mr. OBEY. Good morning. The hearing this morning is going to focus on the Administration's budget request before us as it deals with the environmental challenges facing us worldwide.

There are many anniversaries coming up in April. This happens to be the 21st anniversary of my swearing in as a member of Congress.

I was elected on April Fool's Day and sworn in on April 3rd. It also is approaching the 20th anniversary of Earth Day.

Twenty years ago, I think it's safe to say that in any discussion of Third World economic development programs, the effect of those programs on the environment would not have been given a significant thought in the halls of Congress or, certainly, in the White House. In fact, we managed to get through the 1968 campaign for President with none of the Presidential candidates devoting a significant speech to the subject of the environment.

Today, by contrast, I think it's generally understood that it would be irresponsible to consider aid programs without considering the impact of those programs on the world's environment and the ecosystem, whether we are talking about energy or whether we are talking about deforestation, population growth, agriculture, or pollution of aid programs. They all impact significantly on the condition of the world environment, and that applies both to our bilateral and our multilateral programs.

They can have both a negative or a positive effect on the environment. Later today, we will hear Administration testimony in which the Administration will lay out how they believe their budget request will deal with the environmental problems that confront us.

Before we hear from the Administration, we will hear from a panel of environmental experts, from Mr. Scott Sklar, Executive Director, U.S. Export Council for Renewable Energy; Mr. Glenn Prickett, Research Associate, Natural Resources Defense Council; Mr. Michael Wright, Vice President for Wildlands and Human Needs, World Wildlife Fund/The Conservation Foundation; and Geoff Barnard, Vice President of the Latin American Division of The Nature Conservancy.

Before we hear from that panel, however, I have asked Senator Gaylord Nelson, who was the father of Earth Day 20 years ago and is now senior counselor to the Wilderness Society, to simply sketch out for us in more broad terms what he considers to be the overriding challenges which confront us in this area.

In my judgment, I served in the Congress with three outstanding environmentalists in my 21 years in this puzzle factory. One was Scoop Jackson from the State of Washington, another was Ed Muskie from Maine, and in my view the most outstanding of the three is Senator Gaylord Nelson from Wisconsin.

I say that without a bit of bias. His accomplishments go far beyond originating the idea of Earth Day. If you want to see them in concrete form, all you have to do is take a look at my State. If you want to take a look at the issues we are debating today, it is very hard to find an environmental issue that we are debating today that was not originated by the gentleman who is about to make his comments this morning.

I think that more than any other public figure in recent American history, Gaylord Nelson has worked to bring about an understanding of the necessity for an environmental ethic that ought to govern our actions in many fields, including our efforts at economic development.

Let me simply stop at that point and ask you, Gaylord, to make whatever comments you'd like to make.

SENATOR NELSON'S OPENING STATEMENT

Senator NELSON. Mr. Chairman, I didn't have time to prepare a text and send it up here in advance since I've been traveling around the country speaking to college students about the environment and Earth Day.

First, I want to commend the Foreign Operations Subcommittee for concerning itself with the kind of foreign aid that helps developing countries preserve the integrity of their resource base.

This, after all, is the wealth of each nation and the world. It is vital that it be preserved. As we gain more experience in our efforts to help developing nations environmentally, we should aim toward the goal of creating a substantial international environment fund supported by the industrial nations.

Its objective should be to give the kind of advisory technical and financial assistance that would make it feasible for developing countries to utilize their resources profitably but on a sustainable basis.

I would hope we could look to the day soon when foreign military aid and sales would come to an end and those monies would be reallocated to better husband the sustaining resources of the planet.

ENVIRONMENTALLY SUSTAINABLE DEVELOPMENT

The whole world would be better off if the developing nations avoided the mistakes of the industrial world and succeeded in creating an environmentally sustainable economy without first going through a long period of wasteful capital depletion, as we have done here, and are still doing, much to our long term damage.

It's time, I think, that we recognize that for 200 years we have been guided by a development growth ethic that has unqualifiably promoted maximum exploitation of all natural resources without regard to environmental consequences.

The result has been a dangerous degradation of our life sustaining ecosystem. The challenge now before us is to change our conduct as a nation and as individuals in significant ways with the objective of creating an environmentally sustainable economy.

There are no models, since all developed industrial nations have relentlessly pursued a course of degrading and dissipating their capital and calling it progress.

The tragedy is that a major portion of the environmental damage done to the Nation in the name of progress and economic growth has been unnecessary, economically costly and degraded the quality of our lives.

Environmental critics argue that it would cost too much and jeopardize economic growth if we were to adopt measures to prevent further environmental degradation and begin the difficult process of restoration.

They fail to recognize that our long established policy of degrading, spending, consuming our natural resource base and charging it to the future will disastrously compromise the economy of future generations and leave them with an environmental deficit they can never pay.

In fact, we are already paying tens of billions of dollars annually to clean up pollution that could have been prevented in the first place at a fraction of the clean-up cost.

In short, we are spending the Nation's capital, its wealth of natural resources, and counting it on the profit side of the ledger. A sovereign country can no more fuel its economy by consuming its capital than a private corporation. Ultimately, both will go bankrupt.

What we are dealing with here is a politically bankrupt slash and burn policy that is economically, environmentally and morally indefensible.

If we are to create an environmentally sustainable economy, which we certainly must, it can only be achieved by a kind of social compact among all the political, social and economic interest groups: government, business, labor, agriculture, academia, the religious community, and the general public.

This objective can only be achieved by a massive cooperative effort. Continued confrontation on every front on every issue will not work, is counterproductive and no longer necessary.

There is, finally, a pretty general recognition that the environmental situation is grave and must be addressed. There will, of course, be confrontations, disagreements and constant debate, but for the most part the confrontations in the future will not be over whether something needs to be done, but rather about how much, how fast, and by what means.

This is not to suggest that such a compact will spring forth fully matured this year or next, but rather that all the elements of a compact are clearly visible on the horizon and its time must come, the sooner, the better.

If we were all asked the question what in the long run is the most important issue facing mankind on the planet, how would we answer?

Well, if you think carefully about it, there's only one issue that stands alone above all others right now and in the long haul into the next century and the centuries thereafter.

No other issue is more relevant to the condition of human life than the status of our resources: air, water, soil, minerals, scenic beauty, wildlife habitat, forests, rivers, lakes, oceans.

It is this resource base that defines the habitat and limitations of survival for all species, plant and animal, including humankind, and it also determines our standard of living as well.

Indeed, these resources determine quite precisely the condition of our lives on the planet and influence quite dramatically the human condition physically, spiritually, intellectually and philosophically.

There is, quite simply, no other issue with a more compelling entitlement to our attention and our time, and yet, strangely, this issue which is of fundamental consequence for this and all generations plays a secondary role to a multitude of less important issues.

The resiliency of the living planet has already been dangerously compromised in many places. It is rapidly losing its capacity to renew itself.

The insults to the land, water and air are too many and too massive. In short, the threads of the net that hold the world ecosystem together are breaking and unraveling.

NEED FOR COORDINATED WORLDWIDE ENVIRONMENTAL EFFORT

Only a major coordinated worldwide effort will save what is left of the natural world and give nature a chance to repair some of the damage we have caused.

It is time our leaders recognize that the threat to our environment is far, far, far more important, far more insidious than the threat of nuclear war, missile gaps, Star Wars, crime on the streets, the National debt, the foreign trade deficit, world hunger, the current state of the economy, or any number of other issues that occupy the front pages of our daily newspapers.

There are literally dozens of important environmental issues to be addressed. Some are more important than others and some more urgent, but there is no general agreement on what the priorities should be.

Everyone has his or her own special list. Only the President has the power and prestige to select a National agenda of priorities and rally the country to support it.

During the campaign, the President characterized himself as an environmentalist. We were cheered by that. We all truly hope he will turn out to be a genuine environmental leader on the National and world scene.

Indeed, the opportunity is here right now. We are at one of those rare points on the timeframe of history when a remarkable combination of events has come together opening a window of opportunity for Statesmen with vision and courage to seize the moment and change the course of history for the better.

What is needed right now is strong, vigorous, and imaginative leadership from President Bush and President Gorbachev.

They have it in their power to alter dramatically the course of history if they will but grasp the opportunity. The cause is right, the time is right, the world is ready.

Mr. Bush and Mr. Gorbachev should begin by formally declaring to the world an end to the Cold War and the beginning of a new era.

The Soviet economy is a shambles. It desperately needs relief from the burden of unproductive military expenditures. So does the United States.

The National debt overhangs the economy, saps the vitality of our whole economic and social system, weakens our competitiveness and distorts National priorities.

Both nations would benefit from a drastic reduction in military expenditures and a reallocation of resources to the environment and other socially productive enterprises.

President Bush would inspire the world and give it the dramatic leadership it yearns for if he would propose that the United States and the Soviet Union mutually reduce military expenditures by 50 percent in the next 10 years and another 50 percent in the following decade, with half the annual savings allocated to husbanding the ecosystem of the planet.

Under this proposal, everyone is a winner. There are no losers. This is not unilateral disarmament, it is not idealism run amok, it is plainly and simply hard-nosed realism.

How much longer are we and the Soviet Union going to expend a total of $600 billion a year on weapons systems that ironically put us both in greater jeopardy every single year than we were the year before while degrading and destroying the very resource base that sustains us?

Once Mr. Bush and Mr. Gorbachev reach an agreement in principle, the Iron Curtain countries, western Europe and most other nations could be persuaded to follow because it would serve their best interests, too.

Now, for the first time, the Nation is confronted with a challenge far, far more serious than any war or any economic depression in our history.

Mr. Bush has a golden opportunity to grasp this issue and lead the world. The United States is the biggest industrial power and the world's greatest polluter.

This Nation has an obligation to set the example. Whatever else President Bush may do in his presidency will fade into distant memories, but if he successfully initiates the battle to preserve the integrity of the planet, he will be remembered as long as history is written.

It's a rather interesting coincidence to me that in the past year something has happened that I talked about on April 21st at the University of Wisconsin on the day before Earth Day in 1970, in which I stated at that time we are a creative society with a great capacity for inventing reasons why we can't live with the Russians.

The Russians are equally creative inventing reasons why they can't live with us. I suggest that neither of us will survive in any acceptable condition unless we are prepared to put our petty war games aside and start dealing with matters that are important to the human enterprise. Thank you.

Mr. OBEY. Thank you very much. I know you have to catch a plane, so I will keep the questions short. I want to just ask three.

ADMINISTRATION'S BUDGET REQUEST FOR ENVIRONMENT PROGRAMS

You indicated that you think that the number one challenge before us is to try to deal with the problems of our resource base and the abuse of that resource base.

How well would you say the budget does that? How well would you say this budget does that when it recommends to the Congress that we reduce our support to the United Nations Environment Program by 15 percent and it increases their request for military aid by $300 million this year?

Senator NELSON. Oh, I think what's going on is a tragedy for the whole world. The President, I hope, will turn out to be an environmentalist, but the President has yet to come before the Congress and the Nation and deliver a speech on the environment saying how he perceives the problem, what his agenda is and what he would like to accomplish.

If he did that, I think the whole country would rise behind him. We have for years neglected the environment, which is a very short-sighted policy.

We need to allocate a much larger percentage of our resources to addressing this problem, and it's a puzzler why we don't seem to understand that the greatest threat to this Nation and any other nation on earth is not war, nuclear war.

The greatest threat is the continued deterioration of the environment, the oceans, the rivers, the lakes, the air, the soil erosion, the deforestation, desertification, and the depletion of our minerals.

This is the serious fact. What we really do is operate on the short-sighted policy that it is more popular politically to consume our capital and make people feel rich while they're getting poorer, because they are consuming the capital that accumulated over tens of thousands of years, and we haven't yet come along with a Statesman who would stand up and say "the future of the country is at stake, we must all understand it, and here's the direction we must go."

I would like to see the President do that, and if anybody ever lost an election because he or she did that, at least they would be remembered in history as a person who understood the issue and had the courage and Statesmanship to address it.

Mr. OBEY. My concern is that rather than seeing the initiative that you suggest we ought to have from the President and Mr. Gorbachev, we have the ironic situation in which the reduction of military tensions in eastern Europe has had the perverse and pathological result of having both the Soviet Union and the United States begin the process of trying to dump off surplus military equipment, on both sides of the Warsaw Pact line, to the Third World, by encouraging the Third World to accept military equipment which is no longer needed along the Iron Curtain divisions.

So it seems to me that as much as we need the kind of initiative you're talking about, in fact, so far, the two leaders have been putting a little reverse English on the ball.

Senator **Nelson**. Well, there's enough fault to be spread all over the place, including the Congress, I might say, too, and including the general public.

POPULATION GROWTH AND CONSERVATION

You mentioned environmental ethic. Every time anybody speaks on the environmental question any place one might go in this country, and I suppose in any other country, one question is unfailingly asked, and that is what is the most important environmental issue or issues, and then everybody comes up with a list of them.

I now respond saying let me give you the second most important issue first, and then I don't know how I would rate the third, fourth and fifth, but I would rate as the second most important issue the exponential population growth on the planet.

There isn't any question that we're in trouble now with all kinds of areas on the planet already populated beyond the carrying capacity of the land base that is there.

When I was born, there were a little fewer than 100 million people in America and 1.6 billion people on earth. There are now 250 million people in America and 5.3 billion people on earth.

So I would say that's the second most important question. The first and the most important question, in my view, by far is the lack of a conservation ethic in our culture.

If we're going to address the questions we have to address and we get the political leadership we need, we have to have people who understand what the leader is saying and proposing and agrees with it and supports it.

Until we raise a conservation generation that is guided by an ethic that always asks the question what is the implication of our intrusion here into the environment, since we're all part of the same environment, if we had a generation that asked that question, we would never have ruined the Everglades, because any simpleton could look at it and say this is nonsense.

Lots of people did look at it and say we shouldn't do that, but the Corps of Engineers thought otherwise. If you had had a society in this country and in Florida with a conservation ethic, they would have said this is the greatest fresh water complex of its kind unmatched anyplace on the face of the earth, we're not going to destroy it in order to grow some more tomatoes.

Or if you had that kind of an ethic in our culture, we wouldn't still be destroying 440,000 acres of wetlands every year in this country in order to build more shopping centers or in order to subsidize surplus crops, and then the farmers are draining the wetlands to get more land to grow more surplus crops for crops that are subsidized.

So until we get a generation that has a view that's guided by a conservation ethic, then I don't think any of these major problems could be seriously addressed. Without it, I don't think we can make the transition from an economy that is dissipating our capital to one that is environmentally sustainable as an economy.

So that, in my view, is the most important issue. I would hope that somebody would call this to the attention of the President, and the President, in a message, would say to all the States do what the State of Wisconsin has done.

Mandate that you start environmental education in the kindergarten, all the way from kindergarten through high school.

If we do that in all of our States, we'll create a conservation generation that won't have to spend 10 years piddling around with an acid rain control bill. They'd be sensible enough to pass it in one year.

RAIN FORESTS PRESERVATION

Mr. OBEY. Just one last question. Twenty-five years ago, when I was just out of college, I looked at those rain forests and just figured they were going to be there forever. Now, today, people are wondering whether they can be salvaged at all, given the tremendous pressures on them. You know the way the world of politics works, you know what has happened over the past generation.

If you had to rate our chances of saving the rain forest today, how would you rate those chances?

Senator NELSON. I think it's politically and physically and economically possible to do with some leadership. Look, half the biodiversity, an estimated half of all the biological diversity on the planet, is in the tropical rain forests.

Everybody in all the western industrial developed countries has expressed great concern about the cutting down of the tropical rain forests because of the loss of biological diversity and the effect on the climate and the oxygen that's going into the air.

It affects us. It affects us right here. It isn't just affecting Brazil and the countries that have tropical forests. It's affecting the great wealthy industrial countries of Japan, the United States, England, France, West Germany, Italy, all of them.

They're all complaining. In fact, we've had delegations go down to Brazil and talk with the President about it. He very interestingly said why are you cutting down the last temperate zone rain forest on the face of the earth in the Tongass National Forest and in Washington, Oregon and northern California?

Thousand-year-old trees, five hundred years old, six hundred years old when Columbus got here. Of course, in the climate of the world, they aren't as important as the tropical rain forests are, but as ecological history books, they certainly are, and once they're down, the earth will never see another ancient temperate zone rain forest because it would take 2,000 years to produce it, and there isn't any piece of land on this planet that's going to be left alone for 2,000 years.

Now, if we're so sincere about this, why aren't we doing anything about saving our forests. I've talked about this with Fabio Feldman, a distinguished environmental leader in the Brazilian Congress.

They know that in the long pull slash and burn of those tropical forests is very expensive, very costly to their own economy and that a sustained yield management of those forests would work and be better for the economy.

But they have to eat today, so now if we really are as concerned as we say we are, and we should be, why doesn't the United States and Japan and western Europe say to the President of Brazil, look, we understand your problem.

We know that it will take a transition for you to eliminate slash and burn policy and go to a sustained yield policy of managing those forests and that it will cost your economy money that you don't have and can't afford; therefore, we, the Western world, who have a stake in this, too, will work out with you a plan to do this and come up with the money to offset the losses you'll sustain.

Isn't that an obligation of ours if we think it's so important? It is important. Of course it is. Where is the leadership on that question? I don't see it anyplace.

Mr. OBEY. Mr. Coleman?

Mr. COLEMAN. Thank you, Mr. Chairman.

PUBLIC OPINION AND PRESIDENTIAL LEADERSHIP

I want to thank you for your testimony. I appreciate it. I think the problem is that George Bush is kind of like everybody else in politics.

They all look and see what the polls tell them. The polls I think are telling him that it's good to say you're an environmental president, but to actually do anything that might cost his natural constituency or the taxpayers anything is something he's not willing to do, unless we can borrow some more money.

The press doesn't care. I've got to be real candid. The press right now isn't worried about the national debt, they're not worried about the deficit, they're not worried about the Japanese stock market, they're worried about pact reform and stuff like that.

I'm just kind of frustrated as one member of Congress. I read something by George McGovern this morning about the weakness of my party, the Democratic party, in not taking positions.

Au contraire. We take them. Nobody cares. The reality is America is out there fat and happy. They love everything that's going on.

I'm going to be honest with you. George Bush is not any more an environmental president than he is kinder and gentler. I have 28,000 people in my district without drinking water. I had a provision in a rural agriculture bill that passed the House to permit loans to people that they'll pay back. He said he's going to veto the bill on that.

Kinder and gentler? I don't know. I'm one of those members that just says we're not going to get people's attention on the environment or leadership from the President on the environment unless his polls tell him it's in his best interest to do it and if it doesn't cost anything.

So I'm a little skeptical about us even taking up the issue of the environment in terms of the other States, Senator, and I'm just going to say there's a number of us who feel that way.

Senator NELSON. Well, just one final comment. When I organized Earth Day in 1970, I had one objective in mind, or two objectives.

The main objective was to get a demonstration so big that it would force this issue into the political arena, into the political dialogue, because it wasn't fair.

I was satisfied from speaking in some 37 States in the previous few years that the public was way ahead of the elected officials.

I think they still are. The other purpose was educational. Well, we did get a big demonstration, an estimated 20 million people.

This year will be another, and its purpose again is to reinforce, to demonstrate anew the great concern of the public. This is one way that the public can express its concern about what's going on environmentally, and it will be a huge help.

It's always a slow process. I understand. It's a frustrating process, and it's always easy to make the short term decisions than the long term ones.

I was in office 32 years, so I understand that, but when you go to battle, when you go to the second World War, you make decisions because the survival of the country is at stake, and you do whatever is necessary.

You know, the great leadership of this country has only come in crisis. That's why you got Roosevelt and you got Abraham Lincoln and you got Franklin Roosevelt.

They wouldn't have been great presidents in years when there was no problem. They became great presidents because they confronted a challenge to the survival of the Nation in terms of war, economy, revolution, or what have you.

All I'm saying is our President, this one and any other President, ought to perceive that this challenge is more serious than any challenge that was faced by Washington, Lincoln or Roosevelt.

It's a challenge to how we survive on this planet and what our standard of living will be while we're here. Therefore, if the President would step forward and say that and undertake it, I think the public would follow him.

But even if they didn't, what are presidents for, if not to lead the country in the best possible direction? If they lose an election, so what? You've achieved the highest office that anybody can get anyway.

Mr. Coleman. That's right. We elect the intellectual and moral leader of the Nation who sits silent, and that's a problem.

Thank you, Mr. Chairman.

Mr. Obey. Thank you very much. I appreciate it.

Senator Nelson. Thank you.

Tuesday, April 3, 1990.

PUBLIC WITNESSES

SCOTT SKLAR, EXECUTIVE DIRECTOR, U.S. EXPORT COUNCIL FOR RENEWABLE ENERGY

GLENN PRICKETT, RESEARCH ASSOCIATE, NATURAL RESOURCES DEFENSE COUNCIL

MICHAEL WRIGHT, VICE PRESIDENT FOR WILDLANDS AND HUMAN NEEDS, WORLD WILDLIFE FUND/THE CONSERVATION FOUNDATION

GEOFF BARNARD, VICE PRESIDENT, LATIN AMERICAN DIVISION, THE NATURE CONSERVANCY

CHAIRMAN'S OPENING STATEMENT

Mr. OBEY. If I could ask our panel to step forward. The staff communicated that we would probably have two panels, and I think having everybody together would be better.

I apologize because the Secretary of State indicated he wants to have a meeting at 11:15 this morning, which is going to mess everything up. I have not, frankly, decided yet whether I am going to do it or not. I suspect this meeting will be more useful than that one will.

Gentlemen, we have your statements and will put them in the record. I ask each of you to take about five minutes and simply lay out to us your views about the issues that Gaylord Nelson began to talk about this morning.

I would like to know what you think of the budget presentation that we have before us today with respect to it addressing the environmental problems that confront us all.

What changes in the budget do you think there ought to be? What specific changes in policy do you think there ought to be to make us more effective in attacking issues from global warming to you name it? What do you think are the biggest shortcomings of A.I.D. in dealing with the environmental problems that they have to deal with? What do you think a proper level for funding the United Nations Environment Program would be? Any other comments that you would like to make, please feel free.

Mr. Sklar, why do we not start with you?

MR. SKLAR'S OPENING STATEMENT

Mr. SKLAR. Thanks, Mr. Chairman.

As you know, the Export Council is a consortium of eight renewable energy trade associations. The first point I'd like to make to the subcommittee is that many people, both in the Administration and even some in the environmental community, believe that by pursuing a sustainable or environmental pathway does not necessarily promote business. And you can have a sustainable and environmental pathway and promote private sector.

We're the evidence of that. Fifteen years ago, we had less than a half a billion dollars worth of sales; now we have over $5 billion worth of sales, almost all to the Third World, because that's their best options.

They're not buying big nuclear power plants. They're buying small incremental power, trying to cut their debt. And one of the biggest components of Third World debt, after servicing the debt and after paying for medicines, is energy.

The only way these countries can grow is by cutting imported petroleum and using their local resources intelligently.

As Senator Nelson said, the one way that we can save our resources is, in fact, by developing private sector institutions that it is in our economic interest to protect those resources, and that is achievable.

Unfortunately, very few of the policies of A.I.D. or the international development banks, in practice, are trying to do that. So we're finding ourselves, as an industry, that we believe we can resolve some of the very problems you're trying to deal with at the subcommittee, that we are unable to get the attention or support to do the job.

It's not just the U.S. industry. We just had a meeting in Europe where we set up a consortium of 11 independent solar trade associations from around the world whose main goal is to educate the World Bank and the regional development banks to follow a policy to promote solar and renewable energy.

The good news is this subcommittee has done some good work to set some things in motion: (a) you increased the Science and Technology Directorate's Office of Energy funding, which has created talks with us on how to develop training and education in this area; (b) you set aside five percent at the Ex-Im Bank for renewable energy as a goal, and they haven't committed to the goal, but they are talking with us on simplifying financing; and (c) under another piece of legislation signed into law, we resurrected the OPIC Feasibility Program to promote feasibility studies for renewables.

The bad news, and there's a lot of bad news: seven months into the fiscal year, A.I.D. has not committed to any program funding.

This is seven months in the fiscal year, and I know that this subcommittee has not wanted to micro-manage the Administration's programs over at A.I.D., and from a business standpoint, I also have to tell you we generally don't like micro-management of programs anywhere.

But this committee must micro-manage the programs at AID in environment and energy if they are to do the work, because with a seven-month delay in making decisions, by the time they make any decisions, it will be the end of fiscal year 1992. We'll be through two appropriation cycles, and that is tragic.

The second part of the bad news is that OMB has failed to agree to let OPIC use its money, which is not appropriated money. This is money it gets from its insurance programs, essentially $200,000 to start up a Renewable Energy Pre-Feasibility Fund. And that's bad news.

This is not taking money out of the Federal deficit, this is income that they have and that they want to spend. OMB has failed to make any decisions, does not want to, does not think it's worthy of their time.

Finally, TDP, the Trade Development Program, that was set up to promote, to be the new answer to the U.S. industry in exports has set up such internal criteria that very few renewable energy projects can be funded through TDP.

So we are requesting the subcommittee to do exactly what you did with the Ex-Im Bank, set aside a five percent goal for renewables and energy efficiency and see what they do with it. It would at least start to do some things.

A.I.D./INTERNATIONAL BANK ENERGY PROJECTS

Mr. Edelman's testimony highlights some great progress that A.I.D. has claimed they made in Morocco, Egypt, Pakistan, and India on renewables and energy efficiency.

In Morocco, they've cancelled the Wind Program. Wind water pumping is very important for Morocco that obviously needs water.

It's been cost effective, and basically this was a feasibility and maintenance program to teach people to maintain the technology.

In Egypt, it's a multi, multi million dollar program on renewables, that's very, very haphazard. I can't say they have a stellar record in what they've done. As a matter of fact, I can't tell you anything at the moment.

Pakistan started as a multi million dollar program in energy efficiency and renewables, multi million dollars! And, yes, they've done some energy efficiency training for the utilities, but the fact of the matter is almost all of the money for renewables is being spent on fossil fuel projects, exactly what Pakistan didn't want to do, import fossil fuels.

India, good news. They are doing a reasonably good job in both promoting energy efficiency and renewables in India, but remember the country had a proclivity to renewable energy for a long time.

The news gets worse at the international bank level. I attached a graph to my testimony. We did a study on World Bank and Inter-American Development Bank funding of energy.

What a dismal story. Talking about shepherding the world. Well, in 1989, the World Bank and Inter-American Development Bank spent $4 billion on energy.

Of that, $1.2 billion for oil, gas and diesel. That sure helps them resolve their debt problem, doesn't it? They spent $800 million on electrical grid extension, and that's the fascination with both A.I.D. and the World Bank is grid extension.

The fact is they have shut down eight times a day for energy in most of the developing world, utilities are mismanaged, utilities are used as patronage dumps, and what are we doing? We're building up these things so not only do they go out further, but we double their blackouts. We don't resolve the problem.

Then, of course, they spend $1.5 billion on oil and gas development, which is looking for it, not building projects, just looking for it, and $250 million on administration.

How much do they spend on solar and renewable energy? They spend $29 million, that's with an "m," million dollars. That's just wonderful. That really shows that they know not only how to promote business but how they use the private sector to develop local resources.

ADMINISRATION'S BUDGET REQUEST

The budget that you have before you is absurd, and it's absurd in three basic ways. One, and the most obvious, it is environmentally degrading, and it is environmentally degrading not only in terms of water and air quality, loss of biodiversity that you'll hear later, but the fact is it's ruining the economic potential of these countries to ever climb out of poverty.

They will never climb out of poverty with greater debt or destruction of their resource base, and the U.S. and the Western world finances this cycle. It is stupid.

The second reason this is ridiculous is that the U.S. leads in these technologies, and as I talked to this committee last year, 80 percent of the world's diesel engines are made by Europe and Japan.

That is basically what we're financing, diesel engines around the world, and we're financing them in Indonesia, and we're financing them in the Philippines, and if you ever think that that is a policy that promotes U.S. private sector, it is absurd.

We are the private sector that needs help, we will lead, the U.S. will gain. So will they. The third issue, and the most important, is that if you look at any of the emerging democracies in the world today, whether it be the Philippines, El Salvador, Nicaragua, Panama or eastern Europe, the fact of the matter is that they desperately want these technologies.

In Central America and the Philippines, the insurgencies are in the rural areas where they do not have basic quality of life.

They do not have a light bulb. We can provide them with the light bulb. We can provide them with the refrigeration for medicines.

You don't need a Ph.D. in International Affairs to understand that. What do we do? We finance diesel engines. These people can't get diesels, they can't maintain diesels, and they sit there without energy.

They sit there rusting away, and the only way we can stabilize these democracies is to provide them with intermediate technology that's sophisticated and economic.

I was named to the U.S. Delegation to the Helsinki meetings on the economic security of Europe in Bonn, and the reason was not because the Government thought it was a great idea, but because the eastern Europeans desperately need renewable technology.

They have absolutely an environmental wasteland there. They need a way out. We can provide that. This subcommittee needs to micro-manage these programs, develop set asides and goals in every Federal program that makes sense that isn't moving, and then have strict reporting requirements.

Even with UNDP and some of the other U.N. programs, I believe they should be increased, but with reporting requirements. Let's understand what they're doing.

This week on the Mall is Earth Tech 1990. You will see a demonstration 20 years later where this technology has come. We have an 80-foot wind turbine, we have the best technologies, we have a 42-foot trough like these, 300 megawatts; private-sector financed in California. Potential markets are in North Africa, India, China, those two countries all going toward coal and solar thermal can deter that.

We have demonstrations on utility scale photovoltaic projects. Again, 80 percent of our photovoltaic technology goes overseas, Third World development, communications, lighting, water, refrigeration.

So the point that I leave you with is that we have a development policy that is really, really very disoriented and that what we need from the subcommittee, I think, is some strong words, some monitoring, and obviously some budget increases on the quality of life area and decreases on the military side to get some things moving. Or, what Senator Nelson, we will have a very, very desperate situation.

Thank you for your time.

[The prepared statement of Mr. Sklar follows:]

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American Wind Energy Association

Cogeneration & Independent Power Coalition of America

National Geothermal Association

National Hydropower Association

National Wood Energy Association

Passive Solar Industries Council

Renewable Fuels Association

Solar Energy Industries Association

Volunteers in Technical Assistance

Wood Heating Alliance

TESTIMONY

by

SCOTT SKLAR
EXECUTIVE DIRECTOR
U.S. EXPORT COUNCIL FOR RENEWABLE ENERGY

before

HOUSE APPROPRIATIONS COMMITTEE
SUBCOMMITTEE ON FOREIGN OPERATIONS
HEARINGS ON INTERNATIONAL ENVIRONMENT

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APRIL 3, 1990
WASHINGTON, D.C.

INTRODUCTION

The U.S. Export Council for Renewable Energy (US/ECRE) was formed by the nine national trade associations promoting exports of alcohol fuels, geothermal, hydropower, passive solar, photovoltaics, solar thermal, wind and wood energy technology and services. Our associations of manufacturers, service providers and component suppliers urge the Subcommittee on Foreign Operations to:

> *Direct the US/AID Mission Directors to allocate a percentage of their program resources to assist in training of in-country practitioners, promote development of renewable energy resources and energy conservation in Third World countries.*
>
> *Set aside 5 percent of prior year energy funding of The Department of State Trade and Development Program to be used to finance pre-feasibility and feasibility studies of renewable energy projects.*
>
> *Provide directions accompanying the U.S. contribution to The World Bank and the other multilateral banks to establish renewable energy program set-asides, and report to the U.S. Congress yearly on their funding of renewable energy and energy efficiency.*

The reasons for these requests are quite simple. International development programs have been biased towards large-scale, centralized, conventional energy projects and delivery systems. Increased imports of conventional energy account for an ever increasing indebtedness of the Third World. Energy conservation alone will not meet the growth and expectations of the developing world. Energy production through the intelligent utilization of indigenous renewable resources appears to be the only answer.

Our international competitors have already redirected their development assistance programs to increase the use of renewable energy resources while building their renewable energy industries, in some cases to surpass the United States. The U.S. Agency for International Development published "Renewable Energy Agriculture & Health," which clearly describes a series of cost-effective renewable energy applications — most of which can easily compete today against remote diesel generation and electric grid extension. The development programs of the United States of America must expand these renewable energy applications many- fold to promote real economic growth and curtail profound environmental degradation.

THIRD WORLD RELIANCE

One of the most overwhelming economic issues facing the developing countries is how to best initiate policies to deal with increasing Third World debt. This increasing debt has the potential to undermine our entire world economic system. Yet in the face of this reality, the basic policies of both the U.S. Agency for International Development and the international development banks (which we in-part fund), actively promote increased reliance of fossil fuels and large-scale electrical systems.

The economic arguments for renewable energy development are very clear. Greater use of indigenous energy resources will offset conventional energy imports and decrease debt. Greater use of renewable resources are very labor intensive, and will increase employment. Development of renewable energy resources will increase the rural access to energy, thus stemming urban migration and building rural economies. Use of renewable resources will promote reforestation and decrease the mining of timberland.

US/ECRE commissioned a study in January, 1990, to collect and review information from The World Bank and the Inter-American Development Bank regarding their funding of energy and power projects.

The basis of our request was to review basic funding data to determine the extent of support of conventional energy and power resources compared to the emerging energy technologies. As I have testified before a myriad of Congressional Committees, current international development bank financing practices are biased towards conventional fuels which contribute to greater Third World energy imports and thus greater debt. The report clearly shows funding history from 1980-1988 of both The World Bank and the Inter-American Development Bank. US/ECRE is in the process of commissioning studies on the African and Asian Development Banks which will be published later in 1990. Note that World Bank funding of (non-hydro) renewable energy projects is negligible as shown by the attached chart.

US/ECRE recommends new and innovative financing to promote renewable energy applications. Through the development of "building " techniques to aggregate financing of smaller energy projects and by establishing special financing windows, renewable energy support may be increased significantly. Overwhelming evidence suggests that greater Third World debt may undermine the stability of western economies and continued burning of fossil fuels may dangerously alter world climate. Policies must be implemented to solutions that allow developing countries to lessen their fossil fuel dependency and thus lessen their debt and contributions to global warming. Renewable energy is one appropriate answer and as this report suggests, much needs to be changed at The World Bank and the Inter-American Development Bank to insure greater financing of renewable energy in the near future.

The United States policy ought to be explicit. Development programs supported by the United States government must: 1) Support local resource development, 2) Offset coal, natural gas and petroleum imports and 3) Focus on rural development through renewable energy use and support urban energy development through utility management, energy conservation and model energy privatization programs. Far too much assistance has been given to further conventional energy delivery systems which are notoriously poorly managed and it is time that our country acknowledges this fact.

THE WORLD'S ENVIRONMENT

Many agencies and experts have warned of the profound environmental degradation that has occurred through deforestation and the burning of fossil fuels. While the United States is the primary culprit for world carbon emissions, global deforestation lays at the door of the developing world.

While these two issues are serious, another serious environmental problem is overlooked in the Third World. Due to the lack of emission controls and adequate waste and mining practices, severe health problems are institutionalized through the greater use of coal and fossil plants without environmental control equipment or adequate waste disposal technology. Many cities in the developing world are as bad as the industrialized nations were during our own industrial revolution in the 19th century. The health impacts are too numerous to cite in this testimony.

Deforestation not only contributes to global warming and climate change, but is responsible for desertification and severe flooding of coastal plains. The use of biomass resources to encourage reforestation and the institutionalization of reforestation practices to insure long term energy supply is a sound policy.

Energy conserving technologies such as passive solar architecture or solar hot water heating are essential to displace the need for energy production. The tourist industry uses these technologies as a matter of course throughout the Third World. Now is the time to expand this technical experience to the mainstream of the developing world. Training and access to capital are the only two barriers to expand the use of these new technologies.

Both solar electric (photovoltaics) and wind energy have been proven as cost effective ways to produce electricity for remote applications which include lighting, water pumping/irrigation, refrigeration and communications. Establishment of "bundling" many small applications into large projects for easy financing is critical to move these technologies into rural areas. One of the great environmental problems effecting the developing world is the rural migration to the cities. Only by spurring rural development through greater use of remote power will such trends be stemmed. Greater use of remote irrigation and water pumping can also be one of the answers to deforestation by turning deserts into, again, productive, job creating entities.

The World Bank, USAID, and other multilateral banks appear to be infatuated with large-scale, centralized projects. Most of their funding supports the large-scale use of coal, diesel and even hydropower. Even in our country, the investment community has begun to turn away from very large-scale electric plants to smaller, more modular approaches to electric production. Modular electric plants allow the utility sector to be more responsive to market fluctuations. And quite frankly, if large power plants are not operating to capacity, they aren't very economical.

Most utilities in the Third World are poorly managed, experience great loss of electricity due to "line theft," and as a result are not reliable. Most programs of USAID and the development banks, while acknowledging the problem, still promote the large-scale electric approach. The same could be said of transportation fuels, particularly in sugar producing countries, where ethanol may supplant gasoline as a fleet fuel.

Biomass, geothermal, hydropower and solar thermal technologies produce thousands of megawatts in the United States today. Their use is expanding throughout the world at a rapid rate. Our industrial competitors are promoting these technologies far more aggressively than we are because they sense a lack of resolve to commercialize these applications by the United States. All the renewable energy technologies are more effectively used in smaller applications and fit best in modular production themes.

CURRENT PROGRAMS AND AUTHORITIES

The U.S. congress has been especially sensitive to our industries' needs for export and development assistance. Under P.L. 101-218 recently signed by the President, the Overseas Private Investment Corporation (OPIC) was authorized to resurrect its feasibility program as a way to promote renewables. The Office of Management & Budget has yet to respond to allow OPIC to use its non-appropriated program income ($200,000) for this purpose in FY'90.

In the FY'90 Foreign Operations Appropriations, the Export-Import Bank of the United States (Ex/Im) was directed to set-aside 5 percent of last year's energy funding to finance renewable energy development. Ex/Im is working with US/ECRE to establish a one-stop renewable energy application process for Ex/Im, OPIC, TDP, and AID, thus allowing the U.S. renewable energy industry to receive joint assistance in order to be more competitive in the marketplace through more flexible financing.

In the same FY'90 Foreign Operations Appropriations this Subcommittee requested a $10 million increase in the Science & Technology Directorate's Office of Energy for energy efficiency, renewable energy, and global warming mitigation programs. The Agency has made $5 million available to that office for these three purposes. AID has yet to crystallize their renewable energy program but they have expressed their willingness to work with a US/ECRE industry consortia on technology training and project feasability financing. The Subcommittee, in FY'91, should request an overall $20 million for the S&T Office of Energy in which $5 million should go toward innovative financing development packages, $5 million for training and education in energy efficiency, renewable energy, and global warming mitigation.

In FY'91, the U.S. renewable energy industry needs the Subcommittee to require reports from Ex/Im and US/AID on their progress toward these goals and to establish some practical milestones to measure achievement.

Further, the industry needs some language directed to the Department of State Trade & Development Program (TDP) to parallel the directive to Ex/Im Bank which would require a set-aside goal for renewable energy assistance. Their internal leverage requirements currently are biased against small businesses (which predominate in our industry) and small projects and therefore are not very useful for renewable energy development. Congressional language explicitly directing TDP to consider environmental and renewable energy tied to a set-aside would place the right pressure on TDP to be more forthcoming in this area.

However, large-scale projects have been fostered on the developing world causing wide scale environmental degradation which will have serious health and climate impacts on all the world's peoples. Money is too scarce to be wasted on old views of technology and development. Too many times, the United States attempts to project our view of success through big energy plants or promoting energy schemes that may be unadaptable to a different culture or environment. Renewable resources and energy conservation can easily meet fifty percent of the world's energy needs in an environmentally benign and economically efficient way. We must begin to take advantage of these technological gains as soon as possible.

CONCLUSION

The industrialized countries must begin to set an example to improve Third World indebtedness. The industrialized nations, while establishing policies to curtail their own environmentally degrading practices, must encourage environmentally sensitive development in the Third World.

Sample programs must be established by the U.S. Agency for International Development to promote renewable energy. And while USAID's Energy Office must be maintained at least at the $20 million level, a majority of their activities must be directed towards:

1. *Establishment of feasibility and loan guarantee programs for renewable energy development through a TDP 5 percent set-aside.*

2. *Creation of agressive training programs of USAID Mission Directors and their technical advisors, and of Missions to institute renewable energy programs.*

3. *Enhancement of S&T Office of Energy budget to $20 million.*

4. *Announcement by the U.S. representative to the World Bank and other multilateral banks of new requirements for yearly reporting of funding and initiatives to encourage renewable resource and energy conservation practices.*

In addition, the United States Congress should require an extensive reevaluation of our development programs requiring them to be more pragmatic and more supportive of private sector efforts, particularly when they fit the mission of our development agencies. The U.S. renewable energy industries are losing world market share primarily due to unresponsive and inflexible USAID Missions. Policies must be established to turn this around.

If the Third World is to be steered away from following the poor examples of the industrialized world, it is imperative that the United States use our development programs to encourage the utilization of new technologies and programs. Most of the world does not have the kinds of environmental controls we do in the industrialized world. One way to institutionalize environmentally benign growth is through the use of renewable energy technologies. The United States must encourage this kind of long-term development — and it must begin now.

IBRD ENERGY SECTOR LENDING (in millions) -- FISCAL YEARS 1989-90

		Power Generation							Oil and	Electric		Total	Total
ountry	Description	Hydro	Geo-ther	Coal/lignite	Oil/Gas	Diesel el	Wood	Solar	Gas Dev	TX mission	Admin	IBRD/IDA	Project
Argentina	Yacyreta Hydro	252.0										252.0	2,352.7
Bangladesh	Energy sector reform										175.0	175.0	189.1
Bangladesh	Power distribution									87.0		87.0	121.3
Brazil	Nat. Gas distribution								94.0			94.0	285.0
Cape Verde (1)	Power sector efficiency					1.4				1.5		2.9	5.1
Central Afr Republic	M'Bali River project	16.1							0.2	1.1	0.6	18.0	75.7
Djibouti	Geothermal development		9.2									9.2	38.0
Egypt	Power Sector				98.4					62.7	3.9	165.0	721.3
Haiti	Electricity services				21.0					3.0		24.0	30.1
Hungary	Energy resource development								100.0			100.0	680.0
Hungary	Energy conservation										10.0	10.0	see above
ndia	Sutlej River hyrdo power	437.0								43.0	5.0	485.0	1,474.6
ndia	Maharashtra elec power	222.8								171.2	6.0	400.0	1,344.0
ndia	Petroleum transport								340.0			340.0	1,009.0
ndonesia	Paiton thermal power			339.3						12.7	2.0	354.0	1,117.0
Indonesia	Power sector efficiency	8.0				10.0				292.0	27.0	337.0	597.0
Kenya	Geothermal	40.7										40.7	59.6
Malawi	Energy Resource Development	29.8			1.5		14.3				1.1	46.7	86.9
Mali	Long term energy needs	2.7				4.8				12.6	13.0	33.0	103.2
Mexico	Hydroelectric power	455.0									5.0	460.0	1,440.0
Mozambique (2)	Urban household energy			1.2			3.3	0.3	3.0	7.2	3.1	18.1	50.8
Nepal (3)	Access road to hydro power plant	32.8										32.8	40.0
Nigeria (4)	Refineries rehabilitation								27.7			27.7	439.2
Pakistan (5)	Core energy investment	7.5		0.5	10.0				47.0	57.5	2.5	125.0	4,959.0
Pakistan (6)	Irrigation/elec. transmission									29.0		29.0	50.3
Philippines	Electric power distribution									65.5		65.5	130.0
Thailand	Electricity supply expansion			18.0	72.0							90.0	2,037.0
Tunisia	Petroleum exploration								5.5			5.5	9.0
TOTALS		1,504.4	9.2	359.0	202.8	16.2	17.6	0.3	617.4	846.0	254.1	3,827.0	19,444.9

IBRD LENDING -- FY 1990

		Hydro	Geo-ther	Coal/lignite	Oil/Gas	Diesel el	Wood	Solar	Oil and Gas Dev	Electric TX mission	Admin	Total IBRD/IDA	Total Project
Ghana	5th Power Project									38.4	1.6	40.0	124.8
Nigeria	Power sector maint/rehab.				31.6					31.0	7.4	70.0	154.0

FOOTNOTES (Footnotes explain differences between this table and energy lending figures in IBRD FY1989 Annual Report.)

1 Part of $4.7 million transportation sector loan to improve the efficiency of the transport and power sectors.

2 $3.9 million for stoves, lamps, pots not included in this entry. Total IDA commitment=$22 million.

3 Listed in Annual Report as transportation sector loan, to construct access road from Basantpur to the site of the Arun III hydroelectric power station.

4 Listed in Annual Report as industry sector loan to improve Nigerian National Petroleum Company efficiency, preventive maintenance.

5 $250 million for structural balance of payments adjustment not included in this entry. Total IBRD commitment=$250 million.

6 Part of $34 million agriculture and rural development loan to install tubewells and extend electrification to rural areas.

Mr. OBEY. Thank you very much.

Mr. Prickett?

MR. PRICKETT'S OPENING STATEMENT

Mr. PRICKETT. Thank you, Mr. Chairman.

I'd like to talk about energy efficiency today, but first I'd like to start with a lesson drawn from, of all places, last night's NCAA Basketball Championship.

When one surveys the ominous environmental and financial challenges to continued economic development in the world, particularly the Third World, it's clear that the planet is crying out for a UNLV style fast break on workable solutions like renewable energy and energy efficiency.

Meanwhile, however, the international community, particularly the development assistance institutions, continue to move the ball ever so slowly down the court.

Increasingly, in recent years, international assemblies have recognized the need for substantially increased transfers of resources to the Third World to help confront these challenges.

This subcommittee should be a strong advocate for those increased resource transfers. Under the Montreal Protocol for the reduction of ozone depleting substances, negotiations are already identifying hard numbers on what will be needed to help developing countries finance substitutes for ozone depleting chemicals.

On the issue of global warming, as early as June 1988, government and non-governmental representatives from 46 countries called for a World Atmosphere Fund similar to that described by Senator Nelson.

Last year, Third World Scientists meeting in Delhi called for a similar fund. Consequently, this call was repeated by 17 heads of State, not including President Bush, at the Hague, and by 68 environmental ministers, including Administrator Reilly, at Noordwijk.

No one has tried to put a price tag on such an aid package yet, but let's take a look at energy efficiency briefly, which all sides of the global warming debate, industry and environmentalists alike, recognize as a critically needed near term response that's economically efficient in its own right.

ENERGY EFFICIENCY PROGRAMS

Let's look at a small thought experiment on the global needs for energy efficiency programs. Start with Brazil. To its credit, Brazil has an up and running national energy conservation program in its national electric utility that started in 1985, and the architects of that program feel that within two to three years, that program can begin absorbing up to $100 million annually.

Now, if you expand that goal to the top 10 energy consuming aid recipients, including China, India, Poland, Mexico and others, you quickly reach the $1 billion mark annually.

Now compare that to current aid programs in energy conservation. The World Bank has lent $1 billion for energy conservation over 10 years.

Mr. Chairman, we're an order of magnitude off from where we should be very soon. Now, the lesson to draw from this stark contrast is not that A.I.D., that the World Bank, or that the regional development banks don't understand the importance of energy efficiency.

They do. The Chief Executive Officers of A.I.D. and the World Bank in the last year both said publicly that energy efficiency is a critical development issue, economically and environmentally.

Their institutional structures simply can't deliver. For example, in September of 1989, Bank President Conable in Tokyo, in a major environmental address, said that the World Bank is prepared to "take the lead in a worldwide effort" on energy efficiency.

At the same time, energy efficiency in the end use sector accounted for no more than three percent of a nearly $5 billion energy and industry program.

Meanwhile, the Bank manages a multi donor, $15 million technical assistance program in energy, which spends a considerable amount of its time on end use efficiency but has almost connection with the Bank's lending program.

Clearly, we need institutional reforms at the banks and also at A.I.D. At the World Bank, unfortunately, they haven't recognized this need for reform.

WORLD BANK AND A.I.D. REFORMS IN ENERGY ASSISTANCE

In the last few months, the Bank has been quietly circulating a proposal for a new lending facility similar to IDA to finance environmental projects, particularly those with global implications for global warming, ozone depletion, and biodiversity.

We applaud the Bank's interest in this area, and we agree that the Bank must play a strong role. However, this facility, as proposed, would operate on the same flawed principles and practices that have given us so little progress in the environment in the past years.

To paraphrase a well known figure from the first century, the Bank proposes to pour urgently needed new wine into old and wholly inadequate wine skins.

Presumably, this new facility will continue to hold all planning and documentation secret from the public in its donor and its borrowing countries.

It's also unclear what connection this new facility would have to existing programs in energy and industry and tropical forestry and biodiversity under IBRD and IDA, they are already causing some of the problems that the new facility purports to solve. Again, we urge the Bank to continue working on this idea, but we think they should return to the drawing board, work with other donors and NGOs on a proposal for a more effective, more accountable mechanism than the one they put forward recently.

Fortunately, a model for such reform in energy assistance, at least, is emerging on a limited ad hoc scale, thanks to the initiative, in fact, of A.I.D.'s Office of Energy.

That office has cajoled the World Bank and regional development banks into setting up a very informal working group on the energy sector, called MAGPI, the Multi Agency Working Group on Power Innovation.

In fact, as we speak, A.I.D. has cajoled the World Bank into hosting a seminar in wind energy at the Bank. This group MAGPI, on an informal basis, does collaborative efforts in several borrower countries.

The best example is in India, and Mr. Sklar is correct that there are good things happening in India. In that country, the Bank, in fact, has asked A.I.D. to write critical sections of its background paper on the energy sector.

A.I.D. will be writing a section on environmental impacts of energy development, a section on least-cost investment planning—looking at ways to include energy conservation programs in energy sector investment planning—and a section on the potential for end-use efficiency of electricity.

Concurrently, A.I.D. is also preparing a $15 million technical assistance project for India which will leverage Bank lending.

In that project, A.I.D. will contract consultants to work with power planners in India to look at ways of increasing conservation consideration in power planning.

It will also work with energy intensive industries to identify potential efficiency improvements. This project will leverage potentially a $225 million World Bank loan.

Now, about a year ago, bank staff told us that loan was held up in preparation due to "institutional hangups." The solution here is for A.I.D., with its grant-based programs and its strength in institution building, to get in ahead of time and work to smooth out those institutional hangups.

Meanwhile, A.I.D. is also helping the private sector in India finance development and commercialization of innovative renewable and efficiency technologies.

This is the model of coordination between donor agencies in working with the private sector and NGOs that we should see in all the key countries that A.I.D. has slated to identify.

However, currently, this program is based on the initiative of a few individuals in A.I.D. and the Bank. It should become much more systematic.

A.I.D. should be given sufficient resources to coordinate a formal, donor and NGO working group on power planning and energy efficiency to work in all the key countries.

RECOMMENDATIONS FOR A.I.D. AND WORLD BANK ENVIRONMENTAL ACTIVITIES

Let me conclude with a few principal recommendations from my prepared statement, and also suggest some important questions that I hope the Administration panel will address.

On A.I.D., the subcommittee issued very important instructions last year in the appropriations bill and is to be congratulated, but those instructions are going to require considerable oversight.

A.I.D. was authorized to become involved in key greenhouse gas emitting countries where it does not normally work—Brazil, greater activity in India, Mexico.

It's not clear what A.I.D.'s action plans are for those countries, so the subcommittee should insist on A.I.D. presenting clear action programs immediately in the next several months on what they intend to do, particularly in the area of energy with those countries.

It does appear that the agency has been successful in spending the $15 million earmark for a global warming initiative. In fact, it appears that they have exceeded that amount.

Consequently, it seems in order that that goal for the global warming initiative should be increased to $30 million in the coming year.

Another very important item which the Congress included in last year's Appropriations Act was a call for increased staffing on environment and energy in the agency.

Especially in the energy area, staffing is particularly weak. According to the agency, they have only 20 staff throughout the world trained in energy, and more than half of those are sitting here in Washington.

I was pleased to see that former Acting Administrator Edelman committed the agency to hire up to 20 new staff trained in energy and environment, and I hope that the subcommittee will ask Mr. Roskens if he is willing to rearticulate that commitment.

Finally, on the Office of Energy, that office will play a critical role in coordinating a multi-donor effort. For this reason, the subcommittee called for a funding level of $20 million last year for the office, which hasn't been met.

They brought it up from $10 million, but it's still at $15 million. The subcommittee should reassert its instruction for this year and call for a further increase to $30 million in fiscal year 1991.

At the World Bank, the needed actions were very well summed up in your bill last year and subsequently in recommendations that the Treasury Department succeeded in putting into the report on the IDA-9 replenishment from the Board of IDA.

Essentially, they outlined three areas where the bank needs to improve: coordination of that technical assistance program I mentioned, known as ESMAP, with the Bank's lending program; increased staffing capabilities in energy efficiency; and better work on least cost planning, trying to integrate end use efficiency. So continued funding for IDA and IBRD should be based on demonstrated progress in those three areas.

Finally, on the issue of coordination, A.I.D. and the World Bank should be able to show progress on coordination similar to what they're doing in India in the key countries that A.I.D. is going to identify under the global warming initiative.

Basic questions that I hope the Administration panel will address are:

What efforts is the Administration taking to devise effective and accountable mechanisms for delivering increased funding to the Third World countries?

How these efforts relate to the World Bank's recent proposal to establish a new facility and what offer the Administration is making in terms of support from A.I.D. or support from other U.S. agencies to produce a more effective and accountable mechanism for transferring resources?

Also, as I mentioned, specifically what are A.I.D.'s plans for energy programs in Brazil, India, Indonesia, Poland, China and Mexico?

What are A.I.D.'s plans for staffing increases? What are their plans to educate mission directors and program officers in the missions on the critical importance of the global warming issue, of energy efficiency?

Thank you.

[The prepared statement of Mr. Prickett follows:]

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TESTIMONY OF

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BEFORE THE

SUBCOMMITTEE ON FOREIGN OPERATIONS
COMMITTEE ON APPROPRIATIONS
U.S. HOUSE OF REPRESENTATIVES

APRIL 3, 1990

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I am Glenn T. Prickett, Research Associate with the Natural Resources Defense Council (NRDC). NRDC is a private, nonprofit, environmental organization with over 130,000 members. For more than a decade we have had a program focussing on international environmental issues, particularly the relationship between environment and development. As you know, Mr. Chairman, we have closely followed the environmental performance of the multilateral development banks (MDBs) and of the U.S. Agency for International Development (USAID). At the outset, I would like to thank the Subcommittee for its outstanding efforts in this area in the past. Mr. Chairman, thank you for giving me the opportunity to testify here today on the subject of energy and the environment in development assistance.

I. BACKGROUND

Blessed with relatively low and stable oil prices, the industrialized nations of the world have all but forgotten the "energy crisis" that dominated the policy agendas and the public consciousness of the 1970s. Gasoline lines are a distant memory and national energy priorities are increasingly the subject of environmental, rather than economic debate. However, for many of the world's poorer countries a severe energy crisis persists despite the decline in world oil prices. In cities and villages throughout the Third World, women and children walk greater and greater distances each day to collect firewood for cooking. Government energy planners are increasingly stymied by demands for new energy supplies that grow faster than available capital resources. Energy shortages threaten all levels of society, from wealthy elites to poor peasants.

Energy is a fundamental requirement for sustainable economic development. Compared to industrialized countries, developing nations on average consume an incredibly small amount of energy -- roughly 15%, per capita, of energy consumption in the industrialized world and less than 10% of that in the United States. Rapid growth in energy consumption through the introduction of modern energy carriers -- electricity and fossil fuels -- has been critical to the Third World's economic development. However, despite expectations of continued growth, developing nations will likely consume less than half of the world's conventional energy[1] at the end of this century.

Meanwhile, most developing countries still depend on wood, charcoal, agricultural residues, and other biomass fuels (biofuels) for a substantial share of their energy, over 90% in the poorest countries of Africa and Asia. In many rural areas, due to the high cost of fossil fuels and limited access to electric power, biofuels supply the bulk of energy for households, industries, and agriculture. In urban areas, modern energy carriers are available, but often not affordable for poor households. In most countries fewer than 20% of urban households have access to electricity.

Many developing nations will not be able to afford the expansion of electric power and fossil fuel supplies through which they plan to meet their energy needs. In recent years energy sector investments have accounted for 25% of public investments in the Third World, over 40% in some middle-income countries. At the same time, the financial resources of developing countries are increasingly constrained -- since 1984 the Third World has been a net exporter of foreign exchange to the industrialized countries. The World Bank recently estimated that capital requirements for the power sector alone would run $60-$100 billion annually over the next decade. Current trends suggest that capital flows to the energy sector will be inadequate to meet this need. Costly energy shortages stand to become increasingly common among developing countries in the future.

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[1] "Conventional energy" is commonly used to denote modern energy carriers, including petroleum (fuel oil, gasoline, kerosene, diesel fuel, natural gas, and liquified petroleum gas (LPG)), coal, and electricity derived from these fossil fuels, as well as hydroelectric, nuclear, and geothermal power. The term "conventional" applies primarily to the use of these fuels among industrialized societies. Indeed, in most developing countries, biomass has been and remains the most "conventional" energy resource. Customary terminology describes biomass resources as "traditional" fuels, a label I will avoid using, as it implies a low level of technical sophistication which is not applicable to the advanced biomass systems in use in many parts of the world.

Expanding energy supplies will entail significant environmental costs as well. Energy development has exacted a high toll on public health and the natural resource base in developing and industrial societies alike. Locally, increased energy use in developing countries will exacerbate already severe conditions of air and water pollution, hazardous waste contamination, deforestation, and land degradation. Globally, growth in energy consumption throughout the Third World will contribute significantly to rising atmospheric concentrations of carbon dioxide (CO_2) and other "greenhouse gases" which threaten the stability of the Earth's climate. Developing countries, with fewer of the resources needed to adapt to a rapidly changing climate, stand to suffer disproportionately from the predicted effects of global warming.

A. Sustainable Energy in the Third World

There is a way out of this economic and environmental double bind. Energy planners in all countries often ignore a very simple fact. Society values energy not for its own sake but for the services that energy allows us to enjoy. A kilowatt-hour of electricity, a ton of oil, and a bundle of fuelwood are only important for the light, heat, or motive power that they generate. Therefore, increasing the level of services derived from the energy we already consume is an eminently feasible, although historically overlooked, alternative to increasing energy supplies. Hence, the traditional conception that economic growth demands a corresponding growth in energy supply is not wholly correct. Rather, economic growth demands increased energy services, which can be provided by increasing efficiency of energy use, increasing energy supply, or both.

Historical experience in the industrialized nations over the past two decades provides concrete evidence that energy consumption need not rise in lock-step with economic output. In the U.S., for example, our economy grew by roughly 40% with no increase in total energy consumption during the 15 years following the 1973 oil shock. This impressive record resulted from structural shifts in the economy and wide acceptance of energy efficient autos, industrial technologies, household appliances, and other energy-saving equipment.

Similarly, significant potential exists in most developing countries to improve efficiency in the use and supply of energy. In the industrial sector, the leading consumer of conventional energy in most Third World countries, the World Bank estimates that energy consumption can be reduced by 20-30% through relatively inexpensive investments with short payback periods. Actual technical potential for efficiency improvements in all sectors may be significantly higher. Household fuelwood use can be made more efficient through the substitution of improved cooking systems and the use of modern or more efficient biomass fuels. Electricity efficiency gains in commercial buildings and residences have enormous technical potential, with possible savings in lighting, refrigeration, and cooling systems of 50% or more. Substantial fuel savings in the transport sector are possible through improvements in vehicle fuel efficiency, road and vehicle maintenance, traffic management, and mass transit systems.

Saving energy through investing in energy-efficient, end-use technologies is often cheaper than increasing energy supplies. For purposes of meeting growing demands for energy services, energy made available by improving the efficiency of existing consumption is indistinguishable from new supplies of energy. Experience with "least-cost" energy planning in the U.S. has shown that when potential savings in energy consumption are treated as an energy resource, end-use efficiency improvements often prove to be the least-cost investment alternative.

Similarly, analyses in Brazil and India have demonstrated that investments in state of the art motors, lighting systems, and refrigerators can alleviate the need to construct significant amounts of electric generating capacity, at a fraction of the cost. Improving the efficiency of energy supply, especially in the generation, transmission, and distribution of electricity, is also critical in improving overall energy efficiency. USAID recently estimated that aggressive steps to promote efficiency in the use and supply of electricity can save developing countries $1.4 trillion in power supply expansion over the next twenty years.[2] Energy efficiency improvements make economic as well as environmental sense, and will be essential in helping developing countries meet their energy needs.

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[2] USAID, 1988, Power Shortages in Developing Countries: Magnitude, Impacts, Solutions, and the Role of the Private Sector, U.S. Agency for International Development, Washington, DC, March.

B. Overcoming Impediments

Many developing countries recognize energy efficiency as a critical component of energy policy. Most of the leading Third World electricity producers have established or are in the process of establishing national electricity conservation programs. Nevertheless, energy use in most developing countries remains needlessly inefficient. Energy policies in most developing countries, including energy prices, fail to provide the necessary incentives for energy conservation and investment in energy-efficient equipment. Moreover, informational and financial impediments often prevent consumers from acting on economically attractive efficiency opportunities.

Energy pricing policies are important tools for promoting energy efficiency. Fuel prices and electricity tariffs in developing countries often fall below economically efficient levels. Underpricing encourages over-consumption and jeopardizes the financial position of energy utilities. "Getting the prices right" contributes both to supply and end-use efficiency, creating an incentive for consumers to use energy more efficiently and providing utilities with the resources necessary for efficient operation and management.

However, efficient pricing alone is not sufficient. Market failures obscure the economic signals of prices and limit investments in efficiency improvements even at optimum price levels. Sources of market failures include, among other things, incomplete information on life cycle costs of, and availability of, technological alternatives to energy consuming equipment, inefficient "cost-plus" industrial pricing policies, high import tariffs on efficient equipment, limited capabilities for research, development, and commercialization of innovative technologies, split responsibilities between owners and operators of energy consuming equipment, and limited access to investment capital.

Experience in industrialized countries and a small but growing number of developing nations has shown that comprehensive energy conservation programs can help to overcome these informational and financial impediments. Institutions, both government agencies and private firms, can assist individual energy users in identifying and financing economically attractive efficiency investments. Brazil has established an energy conservation program in its national electric company which in five years has helped that country reduce its annual electricity consumption by approximately 1%. The Philippines, with support from USAID, provides subsidized lines of credit and technical assistance to industries for energy efficiency projects.

Also, government policies can be designed to encourage energy conservation, investments in energy efficient equipment, and local development and commercialization of efficient technologies. Effective policy actions include eliminating energy price subsidies, establishing standards for energy efficiency in buildings and individual appliances, requiring efficiency labels on energy-consuming equipment, and creating favorable fiscal incentives for investment in and commercialization of efficient technologies.

II. A ROLE FOR DEVELOPMENT ASSISTANCE

Financial and technical support from multilateral and bilateral development assistance institutions will be critical in developing and strengthening Third World energy efficiency programs. In recent years, Third World energy institutions -- faced with rapidly growing energy demands, poorly developed domestic capital markets, and dwindling levels of foreign private investment -- have relied on development assistance for more than 50% of their foreign exchange needs. Implementing effective energy efficiency programs will require substantial resources. With development budgets in most Third World nations already stretched to their limits, active participation by the managers of the world's largest energy portfolios will be critical in catalyzing energy efficiency.

The MDBs and USAID have made limited efforts over the past decade to help developing nations establish and strengthen energy conservation programs. However, these initiatives have been given shockingly low priority. For example, the World Bank -- the planet's largest financier of energy development -- has devoted no more than 4% of its energy and industry lending to end-use efficiency. Similarly, end-use energy efficiency programs account for less than 10% of USAID's energy programs. Given the urgent economic and environmental constraints facing Third World energy sectors, the MDBs and USAID should work closely in increasing their support for energy efficiency programs and helping borrowers to integrate those programs into their overall energy sector investment planning.

The following analysis is based on NRDC's research over the past year of the energy programs of the World Bank, the Asian Development Bank, the African Development Bank, and USAID. My testimony today will focus primarily on the programs of the World Bank and USAID. However, I will gladly answer any questions from the Subcommittee on the energy and environment programs of the regional banks. NRDC is working closely with the Treasury Department to prepare a report including recommendations for structural and methodological reforms at the MDBs to facilitate greater bank support for end-use energy efficiency programs. A draft of NRDC's report is currently under review by an international group of nongovernmental colleagues. I will be pleased to the share the final report with the Subcommittee when this review is complete.

A. The Need for Coordinated Action

The clearest message now issuing from all corners of the globe and all sides of the environmental debate is the need for coordinated, global action on the planet's environmental and economic challenges. Central to all discussions of global warming, ozone depletion, loss of biodiversity, Third World debt and other related problems is a realization that governments, international organizations, and citizens must work together more closely. This is eminently true of the issue I am addressing today. Greater cooperation between developing country governments and development agencies will be crucial in the creation of effective energy conservation programs.

Specifically, there is a need for closer coordination between the development assistance agencies. The World Bank, the regional banks, and USAID are all engaged in energy conservation activities, but there is little central coordination between their programs. The U.S. can generate a bigger bang for its energy assistance buck if these institutions work in partnership to strengthen energy conservation programs.

Each institution has its own "comparative advantage" in this area. USAID, with its relatively small, grant-based programs and continuous in-country presence, can be highly effective in helping countries strengthen energy conservation institutions, devise innovative methods for financing end-use efficiency improvements, and adopt innovative approaches to energy planning. The MDBs, with their substantial lending portfolios and considerable policy influence, can help finance large investment programs in energy conservation and end-use efficiency, enhance the stature and credibility of energy conservation institutions, and support difficult policy reforms, including energy price increases and energy efficiency standards.

USAID is attempting to foster closer donor coordination through an informal program known as MAGPI -- the Multi-Agency Working Group on Innovation in the Power Sector. Spearheaded by USAID's Office of Energy, MAGPI includes energy staff from the World Bank, the three regional development banks, and several European bilateral aid agencies. In the last year, MAGPI has initiated a range of joint research efforts designed to foster closer working relationships. In India, for example, USAID and the World Bank will cooperate in a country-wide analysis of environmental considerations in the power sector. The Bank intends to include the results of this analysis in background documentation that will guide Bank lending in India's energy sector.

This consultative model should be expanded and focussed on coordinated efforts to stimulate end-use energy efficiency improvements. Donors should establish a special working group to coordinate support for energy efficiency and conservation activities in individual countries. This working group should also include representatives of Southern and Northern nongovernmental organizations (NGOs) with technical and policy expertise in energy and environment. USAID is currently sponsoring an ongoing dialogue on energy efficiency with NGOs and other donors, informally known as the "Global Energy Efficiency Initiative." This group can serve as a basis for a more formal and inclusive working group, making a special effort to draw on Southern expertise. In order to initiate this process, USAID's Office of Energy should be provided with additional resources to coordinate and manage the establishment of such a working group.

B. The Need for Additional Resource Transfers

Additional financial and technical assistance from industrialized countries will be crucial in helping developing countries address global environmental problems. In recent years, the international community has increasingly begun to recognize the need for such additional funding.

- Ozone Depletion Strong consensus has begun to form on the need for additional assistance to Third World nations in phasing out ozone-depleting chlorofluorocarbons (CFCs) and other substances. Ongoing negotiations on amendments to the Montreal Protocol on Substances that Deplete the Ozone Layer have suggested that $100-400 million will be needed over the next 4 years.
- Global Warming Similar calls for additional funding to help developing countries moderate emissions of greenhouse gases are becoming increasingly frequent. The governments of Mexico and India individually have made proposals to this effect. Several international declarations have stressed the need for additional funding, including the statement of the February 1989 "International Conference on Global Warming and Climate Change," held in New Delhi and attended primarily by Third World scientists. Representatives of the U.S. government have subscribed to a number of these declarations, including those from the 1988 Toronto Conference on the Changing Atmosphere and the 1989 Noordwijk Ministerial Conference on Atmospheric Pollution and Climate Change -- a meeting of environment ministers from 68 countries.
- Biological Diversity Although less clearly defined, the need for additional resources to assist in the protection of biological diversity is no less critical. The World Resources Institute has issued preliminary estimates suggesting that an initial investment of $500 million to $1 billion would be required to establish a system for preservation of tropical forest biodiversity, with continuing annual investments of $100 to $300 million required to maintain the system.

As the world's largest polluter nation, the United States has an obligation and a duty to be a major contributor of this increased funding. It is eminently clear that protection of the planet will require substantially increased U.S. environmental assistance to the Third World, not military assistance as was recently suggested by several senior Administration officials in an extremely troubling article in the Washington Post. This Subcommittee should be a strong advocate for increased concessional development assistance -- on the order of the amounts suggested above -- to combat global environmental problems in the immediate future.

While the need for additional resources to alleviate these global environmental threats has been widely acknowledged, there is no similar consensus on the mechanism for accomplishing this urgent goal. On the one hand, the creation of new institutions has been proposed. For instance, the March 1989 Declaration of the Hague supported by the heads of state of 17 nations -- not, incidently, including the United States -- recommended the establishment of an international environmental super-agency that would, among other things, serve as a conduit for "fair and equitable" environmental assistance. Others, on the other hand, have suggested tapping an existing institution or some combination of extant organizations to carry out this mandate. Regardless of the outcome of this debate, it is clear that a coordinated effort of existing donors will be critical in helping developing nations strengthen energy efficiency programs and take other urgently needed actions. A donor-NGO working group on energy efficiency, along the lines suggested above, will be increasingly critical to coordinate substantially increased bilateral and multilateral funding for energy conservation and end-use efficiency programs.

In this context, I would like to direct the Subcommittee's attention to a surprising proposal being circulated by the World Bank. Just two weeks ago, the Bank quietly called a meeting of major donors in Paris to discuss a proposal entitled, "Funding for the Global Environment." The Bank proposed that donors establish a new concessional lending facility at the Bank, similar to IDA, to fund projects concerning global warming, stratospheric ozone depletion, biodiversity, and other issues of global importance. I would like to submit a copy of the Bank's proposal for the record.

While we believe that substantial additional resources are required for these purposes and that the Bank potentially can be a positive force on these issues, we question the Bank's capability to administer the proposed new fund before substantial environmental reforms have been implemented at the institution. The Bank's track record on environmental issues does not yet provide any indication that it would be an adequate trustee for such a critically important fund. While the Bank has made some progress on environmental issues in the last few years, its has not yet demonstrated its ability to harmonize its lending program with its stated environmental objectives. The Bank has continued to fund highly controversial projects, such as India's Narmada Valley development program, which have long been known to be environmental disasters. Recent and upcoming forestry loans to Guinea and Cote d'Ivoire, for example, have failed to guarantee adequate protection for natural tropical forests.

Confidence in the Bank's suitability to manage such a critically important fund will only emerge when the Bank has demonstrated a commitment to reforming its existing policies and programs, as evidenced by substantially improved performance in actual fact. At a minimum, the Bank should demonstrate progress in the following critical areas, in addition to the energy reforms discussed in greater detail below:

- Existing Programs Must Be Reexamined: The Bank's proposal repeatedly emphasizes that environmental funds will be provided in addition to existing aid programs. The Director of the Bank's Environment Department, representing the Bank at the Noordwijk meeting mentioned above, strongly suggested that only additional funds would be used to address global environmental issues. While NRDC agrees that new funds must be provided for this purpose, we believe that existing programs must also be reexamined. We are very concerned that, unless serious attempts are made to address global environmental issues in the Bank's existing portfolios -- especially through programs such as end-use energy efficiency that are both environmentally and economically beneficial -- it will be difficult or impossible to justify additional funds for these purposes.

- Environmental Impact Assessment While the Bank recently adopted a policy on environmental assessment (EA) of proposed projects, the policy has several disturbing flaws. For example, consideration of global environmental impacts is explicitly excluded from EA analysis, despite the Bank's newly-stated position that global environmental issues are of critical importance. Similarly, structural and sector adjustment lending -- arguably the most important areas of Bank operations -- are categorically excluded from EA requirements. Moreover, the Bank's policy fails adequately to guarantee public participation in the EA process and public access to EA documents -- basic components of internationally accepted practice on environmental impact assessment. The public participation requirements in the EA directive, particularly as they apply to the supposed beneficiaries of Bank lending in borrowing countries, must be considerably more specific to achieve the desired goal. Moreover, the Bank's policy on environmental assessment should be extended to include projects that are purportedly beneficial to the environment, including projects that would be supported by the proposed fund.

o Access to Information The Bank still systematically withholds basic documents on its operations from the public in both borrowing and donor member countries. Even member governments are allowed to view basic loan documents only two weeks before consideration by the Bank's board. The Bank should instead institute a policy that specifically identifies a limited number of precisely defined categories of information that may be treated as confidential by the Bank. All documents not falling in these categories should be publicly available. Documents concerning fundamental physical, institutional, and economic elements of Bank operations should never be treated as confidential and all final loan-related documents should be publicly available at least six months prior to Board presentation. A substantial justification should be required for treating any document as confidential.

C. World Bank and End-Use Energy Efficiency

The energy sector has been a primary focus of World Bank activity since the Bank's inception, second only to agriculture and rural development in cumulative lending. The Bank made its first loan for electric power to Chile in 1948 and has subsequently directed $44 billion, approximately 19% of total lending, toward the energy sector. Currently, the Bank is the single largest source of foreign exchange for Third World energy investments -- in 1989 loans to the energy sector totaled $3.9 billion. Due to this considerable financial leverage, the Bank has unmatched influence over energy planning and decision-making in its borrowing countries. In fact, the financial influence of the Bank extends far beyond the amount of money that it lends. Bank-supported projects typically involve substantial co-financing from private financial institutions and bilateral aid agencies. Private banks considering investments in Third World energy projects often look to the World Bank when determining the soundness of a country's energy sector.

1. Inadequate Attention to End-use Efficiency

In the past year, the World Bank has publicly reversed course on the issue of end-use energy efficiency. One year ago, Bank officials told NRDC that the Bank was not interested in increasing its support for end-use energy efficiency programs in developing countries. According to these Bank officials, such projects were outside the Bank's area of "comparative advantage." Subsequently, as a result of substantial public pressure, Bank president Barber Conable announced at the Bank's September 1989 annual meeting that the Bank would "take an active leadership role" in supporting energy efficiency improvements.

However, the Bank has not yet translated its new rhetoric into operational reality. In 1989, no more than 3% of the Bank's lending in the energy and industry sectors supported end-use energy efficiency programs. At the Bank's own admission, its role in promoting end-use efficiency has been largely limited to encouraging borrowers to adopt efficient energy prices. Loan covenants typically include agreements by borrowers to raise energy prices and the Bank has funded efficiency pricing studies in more than 60 countries. However, a recent Bank review concluded that pricing covenants have been largely disregarded.[3]

Beyond attention to pricing, the Bank has provided extremely limited funding for energy conservation programs. By NRDC's accounting, since 1980, the Bank has supported energy conservation programs in 26 countries through 35 loans totaling roughly $1 billion (see attached table).[4] Several of these loans -- accounting for the bulk of total lending -- have financed efficiency improvements in individual industrial facilities, focussing on the energy-intensive cement, fertilizer, and oil-refining industries. Others have financed the development of energy conservation centers. These centers -- typically government agencies -- are intended to conduct energy audits and advertising campaigns, offer technical assistance to design efficiency projects, and develop energy conservation policy and legislation. Several IDA credits to sub-Saharan African nations have supported the manufacture and distribution of improved cookstoves.

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[3] M. Munasinghe et al., 1988, A Review of World Bank Lending for Electric Power, Energy Series Paper No. 2, The World Bank, Washington, DC, March.

[4] Estimation based on NRDC analysis of World Bank Annual Reports and project reports (Staff Appraisal Reports and President's Reports). Project reports were not available to NRDC for all projects; therefore exact values for end-use efficiency components of larger loans are unknown.

Others have financed efficiency improvements in charcoal production and conservation of fuelwood through improved woodlot management and substitution of modern fuels.

Also, the Bank has issued several lines of credit through financial intermediaries for industrial energy efficiency projects. This model of "on-lending" is highly attractive to the Bank, as it can "move" large amounts of money -- as much as $90 million in Yugoslavia -- and requires less Bank staff-time than the preparation of individual projects. Similarly, the Bank has supported conservation programs in Korea, Thailand, and Kenya in the context of four structural adjustment loans to those countries.

Comparing these projects with overall Bank activity in the energy and industry sectors, one quickly sees the relatively low priority given to end-use efficiency. The total dollar amount of the loans and loan components described above and listed in the attached table is slightly more than $1 billion. This figure represents less than 4% of a total energy program of $26 billion since 1982, and less than 3% of the combined energy and industry programs of $34 billion since that date.

2. Opportunities for Improvement

This Subcommittee, in last year's appropriations bill, made several critical recommendations for institutional reforms at the World Bank and the other MDBs that, if implemented, will significantly increase the banks' attention to end-use energy efficiency programs. P.L. 101-167 instructs the U.S. Executive Director of the World Bank to advocate the following reforms:

- Enhanced staff capabilities in end-use energy efficiency and renewable energy;
- Technical and financial support for borrowers to include consideration of end-use energy efficiency programs in energy sector investment planning;
- Systematic consideration of environmental costs and energy efficiency alternatives in economic and environmental assessments of proposed energy projects; and
- Increased lending and technical assistance for end-use energy efficiency programs.

These instructions have already had a significant impact. As a result of strong advocacy by the Treasury Department, the recently approved report of the Board of Governors of the International Development Association (IDA) -- the Bank's "soft" loan window -- on the ninth capital replenishment of IDA (IDA-9) includes recommendations on all four of these points. The Subcommittee should ensure that the Treasury Department and the U.S. Executive Director to the World Bank continue to advocate these reforms, focussing on the following priority areas.

a. ESMAP and World Bank Loan Operations

The Bank provides considerable technical assistance to end-use efficiency programs in its borrowing countries through the Energy Sector Management Assistance Program (ESMAP). Unfortunately, ESMAP's activities are not well integrated with the Bank's far more significant lending operations. ESMAP's pre-investment work in identifying end-use efficiency projects, strengthening energy conservation institutions, and designing energy efficiency policies and standards could be a basis for substantially increased Bank lending.

Managed by Bank staff, ESMAP is funded by the Bank, the United Nations Development Program (UNDP) and a number of bilateral aid agencies. Funding for ESMAP in 1989 totaled roughly $15 million -- more than 60% from bilateral donors. ESMAP was established to complement the Energy Sector Assessment Program, initiated by the Bank and UNDP in 1980 and charged with preparing energy assessments for some 70 developing countries in the wake of the 1970s oil crisis. ESMAP prepares pre-investment studies for specific projects in the context of these assessments. Also, ESMAP provides a wide range of technical and policy advice to energy sector decision-makers.

End-use efficiency, in both conventional and biomass fuel consumption, has been a significant focus of ESMAP's work, accounting for roughly 20% of all completed and ongoing ESMAP activities. In several countries in Asia, sub-Saharan Africa, and the Middle East, ESMAP is helping design comprehensive energy conservation programs for industry -- typically the largest conventional energy consumer. ESMAP is helping governments develop energy efficiency standards for buildings and individual appliances in Asia, Africa, and the Caribbean. In sub-Saharan Africa, Asia, Latin America, and the Caribbean, ESMAP is engaged in a wide variety of biofuel conservation programs for households and industry.

ESMAP's considerable activity in this area has not translated into significant lending support from the Bank. Where ESMAP has completed studies on industrial energy efficiency -- Ghana, Senegal, Sri Lanka, and Syria -- no direct Bank support has followed. In Ghana, the Bank lent $2 million in 1986 for technical assistance to strengthen the government's conservation agency and perform household energy studies, but has not financed any industrial efficiency improvements. In Senegal, the Bank approved a loan in 1984 for efficiency improvements in one oil refinery, but has not supported any energy conservation work since ESMAP has been active in the country. Coordination between ESMAP and Bank lending has been somewhat better in the fuelwood sector, particularly in Africa. IDA credits to Burundi, Malawi, Niger, and Uganda have financed projects identified by ESMAP's studies. ESMAP is currently implementing a cookstove efficiency program under a Bank energy loan to Ethiopia.

Given this unimpressive record of coordination, it is highly surprising that the Bank often points to ESMAP when asked what it is doing about energy conservation and end-use efficiency. Donor governments put this question to the Bank in the context of the recent IDA-9 negotiations. In response the Bank advanced a laundry list of ESMAP programs -- funded largely by bilateral aid agencies -- as evidence of IDA's support for energy conservation.[5] Although NRDC supports U.S. funding for the IDA-9 replenishment, the Bank's misleading response to donors is extremely troubling. U.S. support for IDA should be based on the Bank's use of IDA funds -- not other agencies' funds -- to support energy conservation programs.

The IDA-9 report contains a recommendation from the IDA governors that the Bank "further integrate ESMAP activities into lending operations."[6] Annual appropriations for IDA and IBRD should be based on demonstrable evidence from the Bank that ESMAP activities in end-use efficiency are leading to substantially increased Bank lending in this area.

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[5] See International Development Association, 1989, "Energy Efficiency and Conservation Activities," Technical Note No. 8, September.

[6] International Development Association, 1990, "Report of the Board of Directors on the IDA-9 Replenishment."

Also, the Bank should expand the scope of ESMAP activities to include key member countries that currently do not benefit significantly from ESMAP. Because bilateral agencies provide the largest share of ESMAP's funding, ESMAP activities have been concentrated in the poorer developing countries -- the leading recipients of bilateral aid. Middle income member countries, such as Brazil, Mexico, Venezuela, Poland, and Indonesia, have not benefited significantly from ESMAP. With more highly developed industrial and energy infrastructures, these countries have considerable potential for end-use efficiency improvements. Moreover, these nations are among the world's largest energy consumers and stand to become the planet's leading greenhouse gas emitters. The Bank should seek to expand ESMAP end-use efficiency activities in these countries. To the extent that bilateral agencies are not interested in funding such activities, the Bank should support similar technical assistance activities through its lending program.

b. Power Sector Investment Planning

The Bank has long required that proposed investments in the power sector meet least-cost criteria. To help borrowers identify least-cost energy investments, the Bank supports investment planning studies, often as components of loan operations. However, power sector investment planning has typically been limited to comparing alternatives for expanding and maintaining electricity supply and has not considered cost-effective demand reduction measures.

Recent experience in the U.S. has shown that investment planning methodologies which allow investments in demand reduction to compete with energy supply options often identify end-use efficiency as a priority investment. This new conception of least-cost planning is based on the principle that, for purposes of meeting a growing demand for energy services, a kilowatt-hour saved by improving the efficiency of energy use is indistinguishable from a kilowatt-hour generated by a new power plant.

The first officially adopted least-cost plan in the U.S. indefinitely deferred all new large-scale generators in the Pacific Northwest.[7] Three successive plans in that region have ranked energy conservation as the most cost-effective alternative for meeting growing demands for energy services. As a result, utilities in the region have developed conservation programs which offer financial incentives for consumers to invest in efficient energy using equipment. Currently, over 40 states in the U.S. have adopted or are in the process of developing least-cost planning procedures that include consideration of conservation programs.

Similar modifications to power sector investment planning in the Third World could help governments and utilities satisfy economic, as well as environmental objectives. It is highly unlikely that energy efficiency alone will be able to offset completely all planned growth in electric generating capacity in any developing country. However, integration of energy conservation and end-use efficiency programs into the power planning process will be critical if developing countries are to avoid power shortages. Moreover, incrementally reducing the requirements for new electric generating capacity will moderate the environmentally harmful effects of power sector development.

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[7] A regional Northwest Power Planning Council has been established under U.S. federal law -- the Pacific Northwest Electric Power Planning and Conservation Act of 1980 -- and authorized to prepare regional investment plans for electric utilities in four states.

Bank assistance in implementing such enhanced least-cost planning methodologies would provide added economic justification for utility- or government-funded energy conservation programs. In the U.S., publicly regulated utilities compensate customers for the added first cost of purchasing energy-efficient appliances. Using utility or other public funds in this way obviates the need for even greater investments in new generating capacity. The Bank should assist borrowers in determining the potential for implementing similar programs in electric utilities, newly created energy service companies, or other public agencies.

As described below, USAID is currently working with utilities in Costa Rica and India's Maharashtra State toward implementation of a power planning model which considers investments in end-use energy efficiency. As a first step, the Bank should work with USAID in applying USAID's integrated least-cost power planning model in a wide range of Bank member countries. Eventually, enhanced least-coast planning should be incorporated into the World Bank's sector and project appraisal work. ESMAP should cooperate in this effort by providing technical assistance grants to perform the assessments necessary to derive specific energy conservation potentials at a state and regional level.

Already, World Bank donor governments have urged the Bank to assist borrowers in integrated least-cost planning. In last year's appropriations bill, this Subcommittee called on the Bank to develop and implement expanded least-cost planning methodologies. Moreover, donor country representatives at the IDA-9 negotiations recommended that the Bank "expand its efforts in end-use energy efficiencies and renewable energy programs and. . .encourage least-cost planning in borrowing countries." Annual appropriations for IBRD and IDA should be based on demonstrable evidence that the Bank is working with its borrowers to include consideration of end-use efficiency programs in power sector investment planning.

Indeed, while the Bank's policy directive on energy lending does not require consideration of demand-side measures in least-cost planning, an April 1989 Operational Directive on "Environmental Policy for Dam and Reservoir Projects" states that

> Design of investment programs for supplying water or energy should consider demand management as well as supply options (e.g., conservation of water and energy, efficiency improvements, system integration, cogeneration, and fuel substitution).[8]

If only to insure the consistency of its own policy, the Bank should revise its existing operational policy on the energy sector to include this significant expansion in the requirements for least-cost planning.

c. Staffing

Making end-use efficiency a World Bank priority will require experienced staff to manage end-use efficiency projects. Currently, the economists and engineers who oversee the Bank's energy lending program have little experience or training in the design and implementation of end-use efficiency programs. In the words of one Bank staffer, "I can count the number on one hand -- and I still have fingers left over." This small staff capability contrast sharply with more than 30 full-time power engineers and over 15 full-time fossil fuel engineers and specialists.

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[8] World Bank, 1989, Operational Directive No. 4.00, Annex B: Environmental Policy for Dam and Reservoir Projects. April.

To increase the Bank's capabilities in this area, the staff of each Bank country department should include an "energy efficiency coordinator." This individual should be responsible for managing loans or loan components for energy efficiency in all sectors, including energy, industry, transportation, agriculture, and household fuel use. These positions should be filled by individuals with experience in the design and implementation of successful end-use efficiency programs. To the extent that new positions cannot be created, an existing energy staffer should assume these responsibilities.

ESMAP should coordinate ongoing training and liaison programs with these individuals. Training programs should recruit outside experts for regular seminars on the latest technical and policy developments in end-use efficiency programs in all sectors. End-use efficiency coordinators would be responsible for insuring that their country department's programs are well coordinated with ESMAP's ongoing activities, and the energy efficiency work of the other MDBs and bilateral aid agencies.

D. Agency for International Development

Last year this Subcommittee issued a strong mandate for USAID to expand its programs in energy efficiency. In P.L. 101-167 and its accompanying report, Congress directed USAID to implement a Global Warming Initiative (GWI) -- funded at least at a level of $15 million in FY 90 -- involving substantial increases in energy and forestry programs. Congress also instructed USAID to take the following steps:

- Target $20 million in FY 90 for the Office of Energy, thereby doubling that Office's current budget.

- Increase the number and expertise of USAID staff in all Missions and Bureaus in the areas of energy efficiency and renewable energy.

- Expand programs in energy efficiency, renewable energy, and energy planning throughout the Agency.

- Focus increased energy assistance on key countries that contribute significantly to global greenhouse gas emissions, and in which USAID-assisted energy efficiency and renewable energy programs can significantly reduce those emissions.

As noted above, USAID has a comparative advantage among donor agencies in providing technical assistance and small demonstration financing to strengthen energy conservation institutions and provide financing for innovative energy efficiency technologies. Through its Missions and its central Office of Energy, USAID has already initiated a limited number of innovative energy efficiency and renewable energy projects. P.L. 101-167 provides specific instructions for USAID to expand this catalytic role, particularly in key countries and countries with large ESF programs.

Based on NRDC's analysis of USAID's Congressional Presentation (CP) for FY 91, it appears that USAID has satisfied Congress's minimum budgetary requirement for FY 90 through a net increase in relevant programs of approximately $20 million. However, it also appears that USAID has so far failed to satisfy equally important instructions in P.L. 101-167. For example the CP does not include any plans to support promising energy efficiency programs in China and Indonesia, both critical key countries. Energy programs in Poland, another key country, will focus almost exclusively on so-called "clean coal" technologies, despite a tremendous potential for end-use efficiency improvements in that country. Also, USAID has not funded its central Office of Energy at the level directed by Congress.

1. "Key Countries"

P.L. 101-167 instructed USAID to submit to the Congress no later than April 15, 1990 a report identifying:

> **key countries which stand to contribute significantly to global greenhouse gas emissions, and in which actions to promote energy efficiency, reliance on renewable energy resources, and conservation of forest resources could significantly reduce emissions of greenhouse gases.**

As I understand it, the Agency plans to identify at least 10 key countries from among the following candidates -- China, India, Indonesia, Mexico, Brazil, Zaire, Poland, Columbia, the Philippines, Pakistan, Egypt, and Central America (treated as a single country).

Shockingly, according to USAID's FY 91 CP, the Agency has no plans to initiate end-use efficiency programs in several key countries. The Agency has no specific energy programs planned for Indonesia, China, and Brazil. However, I understand that the Agency may be planning to hire a forestry expert to be based in Brazil and an energy expert based in Washington to serve as energy coordinator for the Latin American region. In Poland, although USAID is developing $30 million in so-called "clean coal" programs with the Department of Energy, USAID is currently not planning any end-use energy efficiency work. Fortunately, I understand that the Senate Foreign Relations Committee is considering an amendment to the Support for Eastern European Democracies (SEED) Act that would direct USAID to devote at least $20 million for energy efficiency activities in the region. I urge the members of the Subcommittee to support this amendment.

USAID's experience in supporting energy efficiency programs should be brought to bear in Poland, Indonesia, China, Brazil, and other key countries. USAID has helped establish national energy conservation programs in Egypt, Pakistan, and Morocco. In four of the ASEAN countries, USAID is funding the development of energy efficiency standards for commercial buildings. In the Philippines, USAID is supporting a subsidized loan program for energy efficiency investments. USAID's PACER program in India is supporting commercialization of innovative energy efficiency technologies and techniques. In Costa Rica, USAID is performing preliminary assessments for the development of a major energy efficiency initiative in all sectors.

USAID's expanded energy efficiency activities under the GWI should focus on all end-use sectors, including industry, transportation, agriculture, and commercial and residential buildings. To date AID has not been active in truly effective energy conservation programs in the transportation sector. USAID should devote special attention to developing efficiency projects in the transportation sector that achieve significant fuel savings through cutting-edge techniques successful in the U.S. and other industrialized countries. In designing these projects USAID should rely on experts with broad experience in the design and implementation of highly effective transportation fuel efficiency programs.

2. Least-Cost Energy Planning

USAID, through its Office of Energy, is assisting a number of countries improve power sector investment planning. Currently, the Office of Energy is helping Costa Rica and India's Maharashtra State employ a newly-developed, investment planning model which allows energy efficiency and renewable energy resources to compete with conventional energy resources for energy sector investment funds.

P.L. 101-167 calls for expanded USAID assistance in least-cost energy planning. The Office of Energy should work with USAID missions, the World Bank, and NGOs with relevant expertise in key countries and countries with large ESF programs to implement USAID's new power planning model, beginning with expanded work in India. USAID should also pursue application of its new power planning model in other, non-key countries, such as Thailand, which could serve as effective models for other countries.

3. Staffing and Training

New U.S. direct-hire staff will be critical to managing increased USAID energy efficiency programs. P.L. 101-167 specifically instructs USAID to increase the number of direct-hire personnel with expertise in energy and environment and authorizes USAID to use program funds for this purpose. NRDC was pleased to see that former Acting Administrator Edelman, in a March 12 letter to Senator Leahy, committed the Agency to hiring up to 20 additional environment and energy staff. We were also pleased to learn that the Agency is developing long and short term training programs for its Mission and Washington staff. The Subcommittee should ensure that Administrator Roskens is also personally committed to these hiring and training targets, and that USAID's new staffing complement will include individuals with experience in the design and implementation of successful end-use efficiency programs.

The Agency should also expand training programs for host country energy sector officials and line agency staff. The Office of Energy's training activities should be expanded to allow key country energy policymakers to meet with U.S. energy sector officials involved in successful conservation and energy planning programs. For example, USAID should sponsor training programs for developing country electric utility officials with U.S. counterparts who have considerable experience in least-cost planning and utility-sponsored conservation programs. NRDC has worked closely with these officials and would be willing to advise USAID on establishing such a training program. Similar exchanges should be established for officials in the transportation and industrial sectors.

4. Office of Energy

The Office of Energy will be a major resource of staff expertise for USAID in carrying out the energy programs described above. To provide the technical assistance necessary for expanded least-cost planning activities, institutional support for efficiency and renewable energy programs, and catalytic demonstration projects in these areas, the Office of Energy will require significant expansion. The Conference Report accompanying P.L. 101-167 stated "that funding for AID's Office of Energy should be targeted at $20 million in FY 90". USAID has not met this target. The Agency's FY 91 CP lists the Office of Energy's FY 90 budget at roughly $15.4 million. While this represents a slightly more than $5 million increase over the FY 89 budget, it nevertheless clearly falls short of the congressional target. Moreover, the CP proposes to then cut the Office's budget by roughly $2.1 million in FY 91. The Subcommittee should send a clear messages to the Agency that the seriousness of the global warming issue demands much more than a one year commitment. The Office's budget for FY 90 should be increased to meet the congressional target and further increased in FY 91 to $30 million. Also, USAID plans to continue funding the Office's Conventional Energy Technical Assistance Project in FY 90 and FY 91, although the CP obligates no funds for this project after FY 90. The Subcommittee should ensure that this project will focus on the improvement and rehabilitation of existing conventional energy systems, and not on capacity expansion.

III. CONCLUSION

International consensus currently emerging on needed actions to combat the related threats of global warming and stratospheric ozone depletion includes a recognition that substantial additional resource transfers to the developing world will be crucial in defending the environmental integrity of the planet. As improving relations between East and West allow us to devote greater attention to urgent environmental challenges, we must not forget that the North -- as the world's primary source of pollution -- has global obligations. Specifically, the United States should recognize that the earth's future -- as well as our own -- will depend on substantially enhanced assistance to developing nations in reconciling economic growth with environmental protection. This Subcommittee should be a strong advocate with the Administration and within the Congress for increased concessional assistance for this purpose.

At the same time, the Subcommittee should continue to play a leading role in calling for environmental reform at the multilateral development banks and USAID. In the past year the World Bank and USAID have both publicly acknowledged that energy efficiency is a critical development issue that deserves high priority in development assistance portfolios. However, neither institution has yet translated this stated commitment into operational reality. Continued oversight from this Subcommittee will be crucial to ensuring that energy efficiency becomes a central priority in the energy programs of these institutions. Specifically, the Subcommittee should focus its oversight on the following areas:

- Donor Coordination USAID should take the lead in establishing a formal donor-NGO working group on energy efficiency. This group should serve to coordinate donor energy programs in borrowing countries to ensure maximum effective support for end-use energy efficiency programs. In this coordinated effort, USAID and other bilateral agencies, through grant-based technical assistance, should help countries establish and strengthen energy conservation institutions and assist in pre-investment work to identify funding opportunities for innovative energy efficiency technologies. These pre-investment activities should leverage much larger resources from the MDBs to finance energy efficiency investment programs. This working group should draw extensively on Southern nongovernmental expertise on this issue.

- Reforming World Bank Energy Priorities Annual appropriations for IBRD and IDA should be based on substantial Bank progress in the following areas, all of which have been clearly identified in P.L. 101-167 and the Report of the IDA Board of Governors on the IDA-9 replenishment: (1) closer integration of ESMAP's pre-investment work in end-use efficiency with the Bank's lending program, (2) cooperation with USAID and NGOs in helping borrowers include consideration of end-use efficiency programs in power sector investment planning, and (3) increased staff capabilities in end-use energy efficiency and renewable energy.

- Implementing USAID's Global Warming Initiative USAID should develop projects to support promising end-use energy efficiency programs in the key countries of Brazil, China, Indonesia, and Poland. Existing energy efficiency, renewable energy and power planning work in India should be substantially expanded. The Agency should cooperate with the World Bank and experienced NGOs in helping key countries include consideration of end-use efficiency in energy sector investment planning. The Agency should act on the commitment of former Acting Administrator Edelman to hire at least 20 new energy and environment staff, including individuals with experience in end-use efficiency. The Agency should increase the Office of Energy's budget for FY 90 to $20 million, in keeping with Congress's instruction, and further increase that Office's budget in FY 91 to $30 million.

WORLD BANK END-USE EFFICIENCY PROJECTS[1]

(amounts in $ million)

I. Project and Sector Loans

Country	Year	Amount	Description
Africa			
Ghana	84	6.9*	petroleum refinery rehabilitation
Burundi	85	12.3*	dissemination of improved charcoal cookstoves
Ethiopia	86	16.0	production of crop residue briquettes, wood waste charcoal, and cooking efficiency studies
Mali	83	7.6*	sugar industry efficiency improvements
Malawi	89	46.7*	manufacture and marketing of improved charcoal kilns
Mozambique	89	22.0*	substitution of conventional fuels for woodfuel and charcoal in urban households
Niger	88	0.0[2]	manufacture and marketing of improved wood, kerosene and LPG stoves, improved fuelwood management, and applied solar energy research
Senegal	86	2.0	household energy studies, conservation institution building (c.i.b.)
Somalia	88	0.09	manufacture and marketing of improved cookstoves
Asia			
Bangladesh	83	2.0	refinery rehabilitation, industrial audits, c.i.b.
Bangladesh	88	11.4	line of credit for industrial efficiency improvements, c.i.b.
China	85	87.0	rehabilitation of 5 fertilizer plants
India	86	198.5	rehabilitation of 7 cement plants
Indonesia	88	21.0	fertilizer plant efficiency improvements, c.i.b.
Thailand	85	7.3	petroleum refinery rehabilitation
Europe, Middle East and North Africa			
Cyprus	83	3.7	industrial audits, c.i.b.
Jordan	84	3.0	industrial audits, c.i.b.
Hungary	83	40.7	line of credit for industrial efficiency improvements, c.i.b.
Hungary	86	25.0	line of credit for industrial efficiency improvements, c.i.b.
Hungary	89	110.0*	updating of national energy conservation program

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[1] Includes all IBRD and IDA projects with components that support energy conservation and end-use efficiency programs. Dollar amounts represent end-use efficiency components. Total loan amounts given only for projects (indicated by asterisk) whose component breakdown is unknown.

[2] The Government of Denmark (DANIDA) provided $11.6 million for the household energy component of this project to be administered by the Bank.

WORLD BANK END-USE EFFICIENCY PROJECTS (CONT.)
(amounts in $ millions)

I. Project and Sector Loans (cont.)

Country	*Year*	*Amount*	*Description*
Pakistan	83	2.4	refinery efficiency improvements, c.i.b. within refinery industry
Pakistan	85	5.0	industrial audits, c.i.b.
Pakistan	87	16.0	refinery efficiency improvements, feasibility studies for future projects
Pakistan	87	87.9	modernization of 6 cement plants
Portugal	82	27.7	industrial audits, c.i.b.
Tunisia	86	4.0	c.i.b., low cost demonstration efficiency projects
Turkey	81	104.0*	efficiency improvements in four fertilizer plants
Turkey	87	35.0	industrial audits, c.i.b.
Yugoslavia	87	90.0*	industrial audits, line of credit for efficiency improvements and manufacture of energy-saving equipment
Latin America and the Carribean			
Argentina	81	10.0	line of credit for industrial efficiency improvements, c.i.b.
Argentina	81	216.0*	refinery conversion, petroleum pricing reform, industrial audits
Barbados	81	6.0*	commercial and industrial audits
Barbados	82	1.1	c.i.b.
Panama	81	1.0	pilot energy audits in several industrial subsector, c.i.b.
Peru	85	4.0	c.i.b.
Total Amount		*1,233.29*	

Sources: World Bank Annual Reports, Staff Appraisal Reports, and President's Reports

II. Structural Adjustment Loans

Country	*Year*	*Description*
Korea	81, 83	First SAL supported energy price increases, energy audits, public promotion, and c.i.b. Second SAL supported audits and technical assistance as well as formulation of building codes for the commercial sector.
Thailand	83	SAL supported energy price increases and industrial audits.
Kenya	82	SAL required that government analyze potential energy savings in industry and transport.

Source: Internal World Bank Memoranda

The World Bank

FUNDING FOR THE GLOBAL ENVIRONMENT

Discussion Paper
February 1990

I. BACKGROUND

1. In recent years a strong consensus has been forming within the international community on the need to intensify efforts in all countries to protect the global environment. The industrial countries, which account for the major share of global pollution, bear a special responsibility for action to improve the situation. At the same time the developing countries are increasingly aware of the threat which environmental degradation poses at the local, national and global levels. While a large number of countries, both industrial and developing, have been addressing environmental issues within their respective national boundaries, they have also begun to recognize the commonality of many of their environmental problems, and the interdependence of their efforts to devise solutions.

2. As a result of this recognition, a framework of global conventions on measures to protect the environment is beginning to evolve. The Montreal Protocol on the phasing out of chlorofluorocarbons (CFCs) and the recent Noordwijk Conference on Atmospheric Pollution are indicative of progress towards agreement on the nature, scale and timing of some of the steps which need to be taken. The Intergovernmental Panel on Climate Change (IPCC) Working Group has prepared a preliminary framework for action which calls for a collaborative approach, citing the common responsibility of industrial and developing countries in combating global warming. It is evident that effective participation by the developing countries in these global agreements will be limited by the inadequacy of their financial, managerial and technical resources and will depend in large part on the willingness of the industrial countries to provide the assistance needed to overcome these constraints.

3. There are a number of important programs already underway to assist developing countries in addressing particular environmental issues. Examples of these are the Environmental Program for the Mediterranean and the Tropical Forestry Action Plan which have received broad international support. Over the last several years, the World Bank has given increased attention to the environmental policies and projects of its borrowers, and is helping them to incorporate environmental concerns into their development programs. A number of instruments are being used in support of this approach including the preparation of environmental issues papers, environmental action plans, environmental assessment guidelines, country and regional environmental studies and environmental projects or project components. Background Note No. 1 describes this approach.

4. Despite these efforts, in most developing countries the project pipeline needed to benefit the global environment is not being built as fast as would be desirable. Many countries, especially those which have high levels of debt, have had to pursue rigorous stabilization and adjustment programs which have sharply constrained resources available for new investments. These countries face difficult judgments on priorities and, in some cases, doubt the wisdom of proceeding with environmentally beneficial investments, particularly those of a global nature, when basic development investments are urgently required. The environmental investments that do occur under these circumstances tend to be limited to redressing environmental difficulties of local or national concern.

5. There is increasing awareness of the interdependence of measures to protect the environment at both the global and national levels and measures to promote development and alleviate poverty. During the last three years, the Development Committee has discussed environmental matters on several occasions, paying particular attention to the progress that the World Bank is making in

integrating environmental issues into its economic policy and operational work. At the September 1989 Development Committee meeting, the Bank was asked to prepare a report assessing the requirements for additional funding for the environment and outlining the possible mechanisms for mobilizing and managing such resources. This request was in response to a general proposal by Germany and others that the Bank review alternative funding mechanisms, and a specific proposal by France for a separate environmental facility, additional to IDA, located within the Bank. France proposed a facility of about SDR 1 billion, and indicated its readiness to contribute FF 900 million over a period of three years. It called on the Bank to explore the possible modalities of such a Facility following the completion of negotiations on the Ninth Replenishment of IDA.

6. In January 1990, following these negotiations, the Bank undertook a series of informal bilateral discussions with potential donor countries who had expressed interest in the possibility of providing supplementary funding for the environment. One of the major questions addressed during these consultations was how to distinguish incremental funding requirements from the needs of on-going Bank and IDA programs. Several donors noted that most of the on-going environment work consisted of national programs and projects to improve local resource management and control and to deal with local environmental degradation concerns. While strongly supportive of these programs, the donors saw little point in adding further to the resources which had only recently been agreed to finance such programs. The case for additional funding was, in their view, based on the proposition that the action plans recently adopted by many developing countries do not give sufficient weight to issues of global concern. These donors identified several different threats to the global environment, and indicated their interest in the development of action programs which could directly address those threats. In this context, additional funding could be considered to alter the incentives facing developing countries in determining the scale and pace of actions that benefit the global environment.

7. This paper has been prepared to facilitate a preliminary discussion among donors of the possible features of a Global Environment Facility. Section II describes the broad areas where action by developing countries could have significant global benefits, and the general content of programs which might be developed in each of these areas. Section III focusses on the modalities of implementing such programs, and in particular the roles which might be played by UNEP, the UNDP and the World Bank in light of the established strengths of each institution. The "pilot" nature of the Facility is stressed and some tentative comments are offered on the potential scale and character of its funding. Finally, Section IV summarizes the issues on which the guidance of donors is requested and indicates possible next steps.

II. ENVIRONMENTAL ACTIONS WITH GLOBAL IMPLICATIONS

8. There is already broad agreement that all countries, both developed and developing, have a common interest in dealing effectively with global environmental problems. But the extent of agreement on how exactly to define the various environmental problems --and, more particularly, on how best to collaborate in addressing them-- varies from issue to issue. This Section examines the current status with respect to four key environmental problems:

- the depletion of the ozone layer;
- the prospects for limiting greenhouse gas emissions;
- the degradation of international water resources; and
- the loss of biodiversity.

Depletion of the Ozone Layer

9. There is a consensus in the world's scientific community --supported by a growing body of empirical evidence-- that the present level of Chlorofluorocarbon (CFC) emissions (and other halons) contributes significantly to ozone deterioration within the stratosphere, and that corrective action is very much in the interest of all nations. Pursuant to the provisions of the Vienna Convention for the Protection of the Ozone Layer, which entered into force in September 1988, several countries--mostly industrial--agreed to take appropriate measures in this regard. The Montreal Protocol, adopted in 1987, is the framework within which reduction in the consumption and production of certain types of CFC's is to be achieved. Following a number of meetings of parties to the Protocol, it has been almost unanimously agreed that there should be a total phase-out of CFC's by the year 2000.

10. The Protocol itself does not specify the assistance, either in terms of technology transfer or financial support, which the developing countries may expect to facilitate their efforts to limit or reduce the production and use of CFCs. At a Ministerial Conference on Atmospheric Pollution and Climate Change in Noordwijk last November, representatives of 67 countries adopted a Declaration on Climate Change which urges all countries to become parties to the Vienna Convention and the Montreal Protocol. In that context, the Declaration goes on to:

> "Urge industrialized countries to use financial and other means to assist developing countries in phasing out their production and consumption of controlled substances as soon as possible, by providing them with sufficient means to enable them to meet their target date. The development of alternative technologies and products in developing countries should be promoted."

11. In preparation for a meeting of the contracting parties to the Montreal Protocol, to be held in London this coming June, discussions are continuing under the auspices of UNEP regarding the possible modalities for assistance to be given to developing countries. A suggestion has been made, for instance, for the setting up of a Trust Fund which would meet incremental costs to developing countries of transition to non-ozone-depleting substances or alternative techniques, in order to assist developing countries to comply with the specific requirements of the Montreal Protocol. With regard to the implementation of a program of assistance to developing countries, the Executive Director of UNEP, Dr. Mostafa Tolba, has raised the possibility of a tripartite arrangement involving UNEP, the UNDP and the World Bank. This concept would exploit the

comparative advantage of UNEP in managing the process of strengthening existing framework agreements and negotiating new ones, and would draw on its acknowledged lead role within the UN system (in close collaboration with WMO) in monitoring of global environmental indicators, research and evaluation of the resulting data. Advice on the technological options available--a critical input to effective action--would also fall to UNEP. The UNDP and the World Bank would operate within the policy framework provided by the contracting parties, taking into account the science and technology-based guidance provided by UNEP. They would be, in effect, the "delivery system"--providing the pre-investment and investment financing support which is needed to take advantage of appropriate technological opportunities. This concept is very much in line with the suggestions for a Global Environment Facility described below (para. 44).

12. Issues of technology development and transfer, intellectual property rights, and CFC phase-out cost estimates for developing country producers will also be important elements in the dialogue between developed and developing countries. But there is little doubt that satisfactory progress will depend on the availability of some funding on concessional terms. While a number of alternative financing mechanisms of an automatic or quasi-automatic character have been suggested, it seems unlikely that there will be early agreement on such mechanisms. Accordingly, the suggestion made in Section III is that initial funding, in what would be a pilot phase, would be provided on a voluntary basis. The aim in the pilot phase would be to test the workability and effectiveness of both the proposals for institutional collaboration and the specific techniques for transferring technology and implementing appropriate investments.

Limiting Greenhouse Gas Emissions

13. The international consensus on the need for limits on greenhouse gas emissions is not as fully formed as in the case of the protection of the ozone layer. The Intergovernmental Panel on Climate Change (IPCC) is expected to issue an interim report in August this year on the scientific evidence concerning the probable extent and consequences of global warming. This will be reviewed at the Second World Climate Conference in November. Once the IPCC completes its work, negotiations on a framework convention on climate change will commence.

14. Response strategies will obviously remain somewhat tentative pending the outcome of the IPCC process. Nevertheless, there is broad agreement--as evidenced, for example, in the Noordwijk Declaration--on several points. First, the industrial countries, because they account for the great bulk of current greenhouse gas emissions, should take the lead in terms of domestic action. Second, to the extent that greenhouse gas emissions correlate with energy use and level of development, the targets for emission reduction by the developing countries need to take account of these countries' legitimate aspirations for sustainable development. Third, priority should be given to actions--such as energy conservation--which make good economic sense even without taking account of the global environmental benefits.

15. The need for assistance to developing countries has been acknowledged only in the most general terms. One reason for caution is no doubt the fact that containment of greenhouse gas emissions stemming from power generation, industry, urban, transportation activities and deforestation is already embodied--at least to some extent--in many activities undertaken by developing countries in the context of on-going development programs. Even when these activities generate acceptable returns in their own right, however, they are unlikely to be undertaken on the scale which would be appropriate if their benefits to the global economy were also factored in.

16. Accordingly, a practical way needs to be found to concentrate special financial support on those cases where a limited amount of new concessional funding could tip the balance in favor of investments which would have significant global benefits. Areas where this may be feasible include:

- the adoption of cleaner fuels and technologies in the energy sector;
- retrofitting and new investments in the power and industry sectors.

17. In many developing countries there is already a trend toward increased reliance on natural gas in the power, industry and household sectors, based on technologies which have become increasingly attractive on economic grounds. Nevertheless, natural gas is not exploited to anywhere near the scale which would be indicated if account were taken of the significantly lower emissions which natural gas creates compared to practical alternative fossil fuels. There are a variety of reasons for slow gas development in developing countries, including complex issues relating to legislation, regulation, ownership, institutional structure and fiscal regimes. The Bank addresses these constraints in its normal operations. But there is no doubt that, in certain cases, an ability to provide somewhat more attractive financing terms for natural gas development--for example, through blending some newly available concessional funds with standard IBRD loans--could make a critical difference in investment decisions.

18. In those developing countries where coal utilization is already substantial and expected to increase significantly in future years (e.g. China, where coal represents about 75% of commercial energy supply), alternative coal burning technologies exist which could greatly reduce greenhouse gas (and other) emissions. The added investment costs of these technologies is a burden which these countries generally believe they cannot afford. There is every prospect, however, that concessional funding to offset the added costs could alter investment decisions and have a significant impact on emissions.

19. These examples are illustrative of the type of activity which could be encouraged without opening the doors to a wholesale re-labelling of on-going programs as "globally significant". Others could be drawn from the transport, urban and industrial sectors. The objective in a pilot phase would be to identify those operations which have a particularly high pay-off in terms of greenhouse gas emissions. Experience suggests that the mere knowledge that new concessional funding would be available for this type of operation could encourage developing country borrowers to consider seriously options which are now effectively ignored.

20. In addition to actions which limit or reduce greenhouse gas emissions, some developing countries are also in a position to increase the absorption of CO_2 through changes in the management of their forest systems. Growing forests, particularly in the tropics, serve as a sink for CO_2 through photosynthesis. This effect is pronounced during the period of intense forest growth when there is a significant intake of atmospheric CO_2. Once a forest matures, it becomes a net releaser of CO_2. Hence what is important is the change in area devoted to forestry. Deforestation releases CO_2 and, on that account alone, has potentially adverse implications for the global environment.

21. Forest conservation, however, is frequently accorded relatively low priority. There may be political pressures to open more land for settlement in the absence of effective programs to promote intensive cultivation. The root causes of deforestation are numerous and complex, and achieving a sustainable use of existing tropical forests or promoting new forest development requires much more than just financial incentives. The Tropical Forest Action Plan, to which the Bank has recently increased its support, illustrates the need for comprehensive approaches.

22. By developing projects to support the demarcation, inventory and sustainable use of tropical forests, the Bank can help countries to improve land use management, ensure the sustainability of forest-based industries, improve the supply-demand balance of fuelwood, conserve the forest ecosystem (cf. para. 28 below), and strengthen local and national institutions responsible for the forestry sector. The attraction of this sort of assistance to Bank borrowers would certainly be enhanced if it were accompanied by additional concessional funding.

Degradation of International Water Resources

23. Transboundary pollution issues affect both the marine environment and bodies of fresh water which are a common resource for more than one country (such as major rivers flowing through several countries). There is as yet no international consensus on these issues, although industrialized and developing countries are collaborating in the UNEP-sponsored Regional Seas Program. This has produced a series of technically sound action plans, but each of these plans faces the problem of attracting the necessary finance. The World Bank, for its part, is supporting regional efforts in the Mediterranean through its Environmental Program for the Mediterranean (EPM), which also draws on the resources of the European Investment Bank, the UNDP, UNEP and the Commission of the European Communities. While still at an early stage, this exercise illustrates the challenge faced in defining an appropriate mix of policy reforms, institution-building and investments which can benefit from a regional approach within each country's set of constraints.

24. As in the case of greenhouse gas emissions, care is needed to distinguish between actions which can and should be taken in the national interest and those which will only be accorded priority if a way can be found to have transboundary benefits reflected in the policy formulation or investment decision. Industrial and urban wastewater pollution abatement programs, which constitute an important share of investments undertaken by developing countries in this area (with external financial support), do have a beneficial impact on marine and freshwater resources. But they primarily benefit the country of origin and, as such, should probably remain outside the scope of a program focussed on the global commons issues.

25. Actions which may deserve support include contingency planning for marine oil spills and prevention and clean-up of toxic waste pollution along major international rivers. Several catastrophic oil spills over the past year have heightened international sensitivity to the need for increased prevention and clean-up efforts on a global scale. For the first time, the international oil industry is promoting a cooperative approach with public authorities in both developed and developing countries.

26. The oil industry and the authorities of developed countries, with the support of specialized agencies such as the International Maritime Organization, should take the lead in resolving the legal, technical and institutional issues associated with oil spill prevention and response. But some complementary investment with Bank support may well be called for in the ports of developing countries to improve their reception facilities for deballasting. Moreover, in view of the need for a quick and coordinated response in the event of emergencies, it will be important that contingency plans are closely coordinated among neighboring countries. While resource needs should be modest, this is the kind of activity which can easily founder for lack of any mechanism to push forward actions which serve the common interest.

27. Toxic waste pollution prevention and clean-up along major international rivers is a similar activity which might be readily promoted through small projects or components of more broadly based Bank-financed operations.

Loss of Biodiversity

28. The World Commission on Environment and Development, chaired by Prime Minister Brundtland of Norway, issued a report in 1987 urging that "serious consideration be given to the development of a special international banking program or facility" to increase substantially "investments in conservation projects and national strategies that enhance the resource base for development." In follow-up to this recommendation the UNDP commissioned the World Resources Institute (WRI) to develop a series of options for achieving the goals set forth in the Commission's report.

29. The WRI Report, issued in September 1989, outlined a number of proposals including one for the creation of an International Environment Facility to further the preparation and financing of conservation projects.

Conservation was broadly defined as "maintaining natural resources as the basis for meeting the needs of current and future generations." Such a definition would embrace a significant part of the lending carried out by the international financial institutions. Indeed, the concept of sustainability of resource use is already accepted in Bank operations as an important objective and would not, by itself, justify additional concessional funding.

30. But the more narrowly defined objective of preserving biological diversity and intact ecosystems could justify such an approach based on the benefits accruing to the world community. Many examples exist to illustrate the general point that the earth's endowment of biological resources is a precious asset which needs to be conserved and managed with allowance for the benefits which cannot be captured by the country directly concerned. Species and ecosystems contribute a wide range of goods and services, from harvestable material usable as medicine or industrial products and genetic resources for food production, to regulating the climate and rainfall patterns.

31. The preservation of specific areas to ensure biodiversity conservation competes with other land uses in many countries. Thus the provision of funds on a concessional basis could provide the incentive to take action with respect to biodiversity conservation in the interests of the global community. In some recent cases, it has proven possible to leverage rather modest amounts of external resources through use of debt-for-nature swaps. Small amounts of bilateral aid have also been used in this fashion. During the recent replenishment discussions for IDA9, while there was agreement that IDA should facilitate such transactions, a number of donors expressed concern that the use of IDA resources to purchase commercial bank debt could harm IDA's image. This problem could presumably be overcome if the resources were to come from a newly-constituted Global Environment Facility in which encouragement of debt-for-nature swaps was one of the avowed purposes.

32. In the case of tropical forest ecosystems, the time dimension is crucial since inaction leads to irreversible damage. Recent experience in Madagascar has shown that the availability of concessional finance combined with a sound project approach, in which institutional strengthening is a key element, can move biodiversity projects of international significance up in public investment priorities. The aim in a pilot operation would be to work with scientists to identify and--in collaboration with the governments concerned--to develop action plans for protected areas in a few regions that scientists believe have unusually great biodiversity value.

III. MODALITIES OF A GLOBAL ENVIRONMENT FACILITY

33. The previous Section has reviewed several different areas where there appear to be promising opportunities to support and encourage actions by the developing countries which have significant global benefits. It is of course for the potential donor countries to decide which of these areas deserve special encouragement. While it is clear that international consensus on the need for action is most advanced in the case of steps to avoid ozone depletion, it may nevertheless be appropriate to pursue a broad-based approach even at the outset.

34. There are two main reasons favoring a broad-based approach. First, the identified areas for action are not independent of each other. Forest conservation and development obviously bear on both greenhouse gas emissions and biodiversity loss. Steps to avoid ozone depletion can have important benefits for retarding climate change. Since an important part of effective action will be to address the policy and institutional factors which are needed to ensure that actions supported by a Facility are soundly based and the benefits sustainable, a broad-based approach is desirable.

35. Secondly, the pilot operations envisaged in the areas of greenhouse gas emissions, and preservation of biodiversity, should shed important light on what will actually be needed to achieve progress in these areas. As governments address these issues in the next few years, it will be helpful for them to have more and better information about the costs and benefits of proposed actions, so that the targets established through international negotiation are as realistic as possible and the estimates of the type and scale of support needed by developing countries can be more precisely defined.

36. The core of a possible new Facility would be the availability of concessional funding separate from, and additional to, the resources recently pledged to IDA. A specific proposal to this effect was put forward by France at the last Development Committee meeting. This Section considers the possible modalities for such a Facility, beginning with a review of certain general prerequisites for effective use of any new funding. It then examines potential institutional arrangements, with special attention given to the respective roles which might be played by UNEP, the UNDP and the World Bank. Finally, questions of financing are taken up.

Prerequisites for Effective Action

37. Additional concessional funding will not by itself ensure effective action. Recipient countries will need to be convinced that the actions to be supported by any Facility are consistent with their own development efforts. This means that the Facility's operations will need to be designed to operate within the country's own policy and institutional setting, and not be seen as separate activities of interest only to external parties.

38. Fortunately, a mechanism now exists for addressing environmental issues in a systematic and comprehensive way. Background Note No. 1 describes the multi-pronged approach which the Bank has adopted for incorporating environmental concerns within the on-going process of development assistance. Environmental Issues papers have now been completed for most active borrowers, and Environmental Action Plans for a number. The operations of the proposed Facility would be pursued within this overall framework.

39. Moreover, the developing countries will wish to be assured that pursuit of actions which primarily benefit the global environment will not involve a diversion of aid resources from other activities. The concept of additionality is difficult to apply unambiguously in practice--particularly given the constraints which exist on

overall aid budgets--but it is nonetheless extremely important.

40. The response of the developing countries will also be influenced by the way in which prospective operations are presented. A common theme in the previous Section was the need to find a way for global benefits to be taken into account in policy formulation and investment decisions by the developing countries. By making concessional funding available, the incentives facing the developing country can be modified to the point where the country sees it in its own interest--as well as in the global interest--to take the specified action. The key point is that it is still the developing country which must decide: nothing in the proposed Facility imposes action on the developing countries. Instead, new options are made more attractive than they would otherwise be.

41. Finally, no action intended to benefit the global environment will be effective if it is not based on sound science and an up-to-date awareness of technological options. While the Bank has ample experience in the preparation, appraisal and supervision of investment operations in developing countries, it will need to work closely with others to ensure that global benefits are assessed based on the best available science and that the choice of technology takes account of the best advice available. This leads naturally into the question of the institutional arrangements for a new Facility.

Prospective Institutional Arrangements

42. It would be premature--while the purposes of the Facility are still to be agreed--to enter into any detailed discussion of institutional arrangements. It may nevertheless be useful to set out certain general features as a basis for obtaining preliminary reactions. Three aspects may be distinguished:

- policy framework and provision of scientific and technological advice;
- coordination of donor and other agency actions; and
- funding mechanism.

The key to the successful operation of the Facility will be the effectiveness with which global environmental concerns can be integrated into the overall development strategy and program at the country level. In its management of the Facility, the World Bank would be able to draw on its experience in assisting countries in designing policies and preparing and implementing investment projects to help achieve this integration.

43. Sound investment will require scientific and technological knowledge which is not always available to developing country borrowers. This may be particularly important in the areas of CFC substitution, choice among alternative fuels and power-generating technologies, and pollution abatement technologies. The challenge is to bring together the best available advice in these areas with investment financing.

44. One possible mechanism for addressing this challenge would be to create an environmental policy body which can advise the Bank in its management of the Facility. It would seem natural for UNEP to play a key role in such a body. Given its experience in the negotiation of agreements in the environmental field on a regional and global basis, UNEP is familiar with the range of environmental policy matters which would form the context for the operations of any new Global Environment Facility. UNEP's Governing Council has approved a list of 'areas of concentration' which corresponds very closely to the areas identified in the previous Section as offering promising opportunities for developing country action.1/

1/ Governing Council "areas of concentration":
(a) combating climate change;
(b) combating the depletion of the ozone layer;
(c) management of shared freshwater resources;
(d) control of pollution in regional seas and proper management of their coastal areas;
(e) halting desertification and deforestation;
(f) conservation of biological diversity within a broad socio-economic context; and
(g) minimization of hazardous wastes, through the development of low and non-waste technologies and the environmental sound management of hazardous wastes and potentially toxic chemicals.

45. The preparation and implementation of investment operations which advance global environmental objectives would be carried out by developing countries, drawing on the assistance of the World Bank and UNDP in the normal way. The UNDP has a well-established role in the provision of technical assistance and the financing of feasibility studies. By virtue of its field representation throughout the developing world and the overview it has of technical assistance needs and implementation capacities, the UNDP would bring important strengths to any new Facility.

46. The UNDP is already an active partner with the Bank in several of the areas cited in Section II. Many actions relevant to greenhouse gas emissions will need to be anchored in energy strategy assessments or analytic work emanating from the ESMAP program, of which UNDP is a major sponsor. Mention has already been made of UNDP's role in the Environmental Program for the Mediterranean.

47. By virtue of its involvement in, and financial support for, developing country programs in the areas of natural resource management, energy efficiency, urban development and pollution abatement, the Bank is currently grappling with many of the relevant institutional and policy factors which have a bearing on the effectiveness of environmental actions. The Bank also administers a technical assistance grant program for the environment, where the initial funding supplied by Japan has recently been supplemented by contributions from Denmark, France, Norway and Sweden. Moreover, a major part of Bank lending is of course in precisely those sectors (energy, transport, urban, industry, agriculture, forestry) where the opportunities for globally beneficial investments are expected to arise.

48. The institutional arrangements for a new Facility could thus reflect the proposal put forward by UNEP with specific reference to ozone layer depletion, described in para. 11 above. UNEP would be expected to play a key role in setting the policy context for the operations of a Facility, UNDP would assist in planning and implementing the technical assistance and pre-investment components, while the Bank would take the lead in managing the external financing for investments and in supervising their implementation.

49. All three institutions should expect to play a role in the coordination of donor and other agency activity which bears on the work of the Facility. Donors to the Facility should have an opportunity--perhaps every six months--to come together with the Bank, UNEP and UNDP to assess progress that has been made and to discuss future directions. The Special Program of Assistance for Debt Distressed Africa (SPA) may provide a relevant model for the sort of consultation that is needed.

50. In order to have consistency of approach, it would be important to have strong central direction of Facility operations in the pilot phase. This would suggest a funding mechanism in which at least a major part of the concessional funding would be administered centrally on a multilateral basis. The success of a Facility will depend on its credibility in the eyes of developing countries, which in turn will be influenced by the extent of additionality. For the Bank to enter into a productive dialogue with potential developing country borrowers on global environmental actions, it must be seen as having some money to back up what it is saying.

51. A multilateral core of concessional funding could be supplemented with bilateral funds--perhaps following the model of special joint financing used as part of the Special Facility for Africa. One should recognize, however, that the Special Facility for Africa was financing relatively standard operations in which both the bilateral donors and the Bank had substantial experience. The Global Environment Facility would be much more of a pilot exercise, testing out new approaches and supporting highly innovative operations. To attempt this solely or mainly through ad hoc bilateral cofinancing arrangements would be exceedingly cumbersome if not impossible. But provided a significant core fund is available to anchor the programs and policy dialogue with borrowers, then bilateral cofinancing would be a useful means of ensuring that the program achieves an adequate scale and coverage.

Prospective Funding Arrangements

52. There is no way to estimate with any reasonable degree of precision what funds might eventually be needed to support the types of activities outlined in Section II. Precise goals do not exist--although they may not be far away in the case of ozone depletion. The pre-investment and feasibility work has yet to be done. The illustrative figures cited in the WRI Report--$20 to $50 billion per year over the next decade--suggest that the task is formidable, however defined. For the phasing out of CFCs alone, figures in the range of $200 to $700 million per annum have been cited. Substitution of cleaner coal-burning technology (fluidized bed combustion) could add 15% to the investment cost of power generation. If concessional funds were used to offset the whole of this increment, costs for this type of operation alone could reach hundreds of millions of dollars per annum.

53. The sheer magnitude of these indicative figures underscores the point made earlier: better information, based on actual experience, could be very helpful to governments in setting targets and pledging support for developing country efforts. Such information would be generated through the sort of pilot approach which is envisaged for the Facility. Initial funding would be determined by the donors in light of the priority they attach to immediate action in the areas identified. The French proposal at the last Development Committee meeting envisaged funding for a three year period of about SDR 1.0 billion. This was for the poorest countries only. Since the actions would not be confined to this group, France has suggested that their initial figure be increased to something on the order of SDR 2.0 billion.

54. Can funding on this order--between $400 million and $800 million per annum--be spent effectively over the next three years? Allowing for an inevitable start-up lag, the answer is yes, if donors wish to pursue a broad-based approach. A number of operations in the IBRD/IDA lending pipeline could, with the concurrence of the borrowing country concerned, be modified or broadened in scope to address issues of direct relevance to the global environment. Projects in the power sector utilizing alternative technology or encouraging fuel substitution are examples of what might emerge relatively quickly. New projects (e.g. retrofitting of production facilities using CFCs) would take more time, but could begin to emerge toward the end of a three year period.

55. How might funding on this scale be mobilized? A number of innovative suggestions have been made for non-traditional funding sources. These are briefly reviewed in Background Note No. 3. Whatever their merits in principle, it seems unlikely that they could be activated on a substantial scale in time to finance a Facility over the 1991-1993 period. Hence it seems unavoidable that, for the near-term at least, the Facility will have to be supported by voluntary contributions from interested donors.

IV. SUMMARY AND NEXT STEPS

56. The central issue on which the guidance of donors is required is the definition of the purposes of a possible Global Environment Facility. There are several facets to this. First, there is the question of the areas to be addressed. As the paper notes, the international consensus is most advanced with respect to actions which help to protect the ozone layer. Nevertheless, for the reasons stated in the paper, a broad-based approach is recommended. Is this agreeable and should an attempt be made to cover all four of the areas described?

57. Second, there is the question of the type of operations to be pursued in the areas cited. The paper suggests certain general guidelines designed to differentiate operations which the Facility might support from those which are mainly of local operational interest. While this type of operational policy will obviously need to be refined, does the direction indicated seem appropriate to donors?

58. Third, the pilot character of the Facility is stressed. Do donors agree that this is an appropriate posture in light of the lack of established targets in several areas as well as the lack of proven techniques for providing the types of assistance outlined?

59. The second major set of questions concerns modalities. A number of general prerequisites to effective action are cited and an outline is given of possible institutional arrangements for the Facility. Do donors concur with the respective roles outlined for UNEP, the UNDP and the World Bank? The tentative comments offered on funding suggest a three-year timeframe beginning in 1991, with operations on a scale of $400 to $800 million per annum, financed on the basis of voluntary contributions, of which a major part would be centrally managed. Is this a satisfactory basis for moving ahead, recognizing that the figures will have to be refined as the discussion proceeds?

Next Steps

60. If donors endorse the broad features of a Facility along the lines suggested, the next step would be for the Bank, in close consultation with UNEP and the UNDP, to prepare a paper for the May 8 meeting of the Development Committee, outlining the possible role and principal features of a proposed Facility. The Development Committee would provide an occasion to test the reaction of the developing countries to the concept. If there is broad support, a follow-up paper giving more details on prospective program content, operating procedures and funding approaches would be prepared and circulated to interested donors for a follow-up meeting in late June or early July 1990.

The World Bank Approach to Funding Environmental Activities

Background Note No. 1

Introduction

In recent years, environmental degradation has become a matter of central concern for both developing and industrialized countries. The evidence is increasing that sound environmental management, rather than posing a constraint on the development process, is an essential ingredient for maintaining the natural resource base upon which most nations depend for their continued economic development. In response, the Bank has been intensifying its focus on the environment in the last two years through a newly established internal structure for dealing with environmental issues. In addition, the horizons of projects were considerably broadened in time and scope to accommodate evolving environmental concerns, and collaboration with outside organizations has been increased.

Traditionally, environmental problems have been perceived as those associated with soil erosion, siltation of dams, and the effects of urban and industrial waste disposal on local populations. More recently, heightened attention has been focused on issues of global concern such as global warming, ozone layer depletion, tropical deforestation, trans-boundary movement of hazardous wastes, acid rain, desertification, and threats to indigenous peoples and species. In developed and developing countries alike, governments have been increasingly investing in conservation measures, building ameliorative components into projects, strengthening environmental institutions, and introducing appropriate regulatory or legislative mechanisms.

The World Bank has long stood committed to help in this regard. But the rapidly unfolding events of the past two decades have called for substantially greater attention to environmental matters and a more comprehensive approach than had been previously pursued by the Bank, as public discussion of these subjects has intensified. As a result, the Bank has adopted a multi-pronged approached to incorporating environmental concerns within the process of economic development assistance. This approach can be summarized under four main headings:

(i) Preparation of Environmental Issues Papers

(ii) Preparation of Environmental Action Plans

(iii) Country and Regional Environmental Studies

(iv) Environment in Lending Operations

Environmental Issues Papers

An important thrust of the Bank's environmental policy is to pay explicit attention to environmental issues in country programming and economic policy dialogue with borrowers. The Environmental Issues Paper (EIP) for each country identifies key environmental problems and their underlying causes in that country. They serve to heighten awareness of environmental issues, delineating responsibility for addressing them in that country's operations, and achieving a consistent approach to their solution.

EIPs for most active borrowers have been completed. Priority topics identified in the papers include a wide range of issues: loss of biological diversity; watershed erosion and upland degradation; deforestation; desertification, air and water pollution; urban sanitation and waste disposal; the protection of cultural property; marine and coastal zone protection and water resource management; industrial and hazardous waste disposal; and environmental health. Many of the papers identify the underlying causes of environmental problems, such as population pressures, institutional weaknesses, perverse economic incentives, and uncertainties about property rights.

EIPs are country specific and may differ substantially depending on country circumstances. For example, an EIP prepared for a large Asian country develops its analysis of environmental problems and causes against the backdrop of a large, growing, and mostly poor population attempting to meet its basic needs in an often treacherous climatic setting. The paper describes a situation of enormous peril to the country's resource base and cites population pressure, land degradation, deforestation, water and air pollution, energy issues, and poverty as important areas for environmental action. The study recommends that the donor community and the Bank concentrate on basic institution-building activities -- assistance for training, management and logistical support, and environmental research and monitoring facilities in key areas.

Another EIP prepared for an African country highlights the rapid rate of population growth as a basic cause of the country's environmental problems and identifies broad sectoral issues in agriculture, livestock, forestry, and health. The paper recommends cross-sectoral strategies for education, legislation, institution building, information systems, and the management and distribution of land.

As noted above, the approach taken in EIPs is influenced by the country's characteristics and is very much country-specific. Conceptually these EIPs, which identify key issues, are the first step in the Bank's approach to developing a coherent country environmental strategy. Generally, the EIP is to be followed by a progressively detailed study, culminating in the implementation of environmental projects and policies. These detailed studies are the Environmental Action Plans. In the case of large countries, the EIP may be followed instead by in-depth studies which focus on specific aspects of environmental policy.

Environmental Action Plans

Environmental Action Plans (EAPs) take several forms. The approach naturally varies from country to country, and success depends on the priority the government gives the subject. So far, most plans have been prepared by Bank staff and consultants in close collaboration with governments and with other external agencies and NGOs. For the smaller countries, an EAP can cover a wide spectrum of activities and provide a framework for integrating environmental considerations into general economic and social development programs.

Such plans provide an overall strategy and recommendation for specific actions, with descriptions of the environmental policies, investment strategies, and legislation required. By identifying the country's most urgent environmental needs, they assist decision makers in determining priorities, allocating limited resources, and, above all, building the institutional capacity to handle complex environmental issues. As an example, a synopsis of an EAP carried out for Tunisia is shown in Box 1. EAPs are being prepared for Algeria, Burkina Faso, Ghana, Guinea, Hungary, Lesotho, Madagascar, Mauritius, Rwanda, Turkey, and Yugoslavia. By the end of FY92, the Bank expects to have completed 30 such studies. This will provide a solid information base from which to identify suitable environmental projects and programs.

Country and Regional Environmental Studies

Besides the EIPs and EAPs, the Bank has also been undertaking other country studies

Box 1: An Environmental Action Plan for Tunisia

In the context of Phase I of the Environmental Program for the Mediterranean, a multi-disciplinary World Bank team undertook a pilot environmental study of Tunisia. The country was chosen because: (i) its environmental problems reflect a broad range of issues characteristic of several countries in the region; (ii) of its strong interest and commitment to environmental improvement and protection; (iii) of its relatively small size and population, in view of the scale and complexity of the issues addressed; and (iv) of the availability of local skills and information.

The study set out to review Tunisia's environmental problems, assess their priorities, propose corrective and preventive measures, and recommend an overall approach towards an environmental country strategy. Issues were analyzed and solutions were examined, first on a sectoral basis, and then put in the perspective of nationwide priority actions, taking into consideration inter-sectoral linkages and implications.

The team found that Tunisia's strong commitment to environmental protection and improvement is demonstrated by the considerable steps taken to date and the ongoing efforts by the various entities responsible for the quality of the country's environment. At the same time, however, these entities are fragmented and often have overlapping functions and unclear responsibilities. Moreover, many of the measures taken were erratic actions suffering from the lack of a comprehensive legal framework and from sporadic enforcement.

At the sectoral level, the study identified problems of (i) land degradation arising from inappropriate practices, (ii) critical water resource prospects requiring careful planning and management, (iii) marine pollution from industrial and urban sources, (iv) air, water, and surface pollution, mostly from industrial and power plants, (v) domestic sanitation and solid waste disposal requiring better management of urbanization, and (vi) protection of the historic and cultural heritage.

After analyzing the causal and contributing factors of these problems, the team developed an emergency package of urgently needed measures and an action plan for the short and medium term. The emergency package includes measures in the following sectors: (i) industrial (SO_x abatement and phosphogypsum landfill in Gabes, closing of SIAPE B chemical complex in Sfax, elimination of mercury losses in Kasserine, and chromium recovery in Nefza); (ii) urban (wastewater, solid waste, and hazardous waste management); (iii) energy (oil spill control equipment and training); and (iv) maritime (extension of fishing restrictions, contamination assessment, and laboratory reorganization in Gabes). The study has interpreted the term "environment" broadly, embracing all major factors affecting quality of life. The action plan thus recommends a series of policy reforms (e.g. regulatory and incentive mechanisms) combined with institution building efforts and investment proposals in the various sectors of the Tunisian economy. After it was thoroughly reviewed and discussed, the action plan was endorsed by the Government. In fact, the Tunisian Authorities decided to use the report as the key background document for a donors' conference on the environment to be convened in June 1990.

focussing on particular environmental issues. An example of such a study is provided in Box 2, which summarizes the environmental strategy study carried out for Poland. Such country studies are also being carried out for Indonesia, the Philippines, Nepal, and Brazil. In addition, regional studies focussing on environmental issues in common for a particular geographic area are also being carried out. Some examples of regional environmental studies include the Capital Cities Clean-up Project, which aims to arrest and reverse environmental degradation from rapid urbanization, industrial pollution, and general environmental neglect in the principal cities of Asia and the Environmental Program for the Mediterranean, through which a regional action plan will be implemented to deal with critical issues such as prevention and control of marine oil pollution, integrated water resources management, solid and toxic waste management, and coastal zone management. This program will include support to policy reform, institution building, and project development. Other such studies include the Asia Watershed Sector Review, the Asia Forestry Concept paper, the Sub-Saharan Africa Agroforestry Study, and the Tribal People Policy: Application to Africa. All these studies help provide a basis from which rational priorities for funding environmental activities can be derived.

Environment in Lending Operations

The impact of structural and sectoral lending on the environment is potentially considerable. By their very nature, adjustment credits go beyond the limits of single projects, to affect wide-ranging pricing and other policies which in turn may directly or indirectly affect the environment. In FY89, five of the 27 adjustment credits incorporated significant environmental features. These credits were to Ghana, Gambia, Guinea-Bissau, the Lao People's Democratic Republic, and Pakistan. The EIPs and EAPs, as well as the other studies mentioned above will serve as a basis for policy dialogue and identification of priorities for inclusion in the design of future Bank structural adjustment loans.

With respect to its total lending portfolio, some 38% of all bank loans contained significant environmental components and this percentage is anticipated to increase significantly in the years ahead. A wide range of environmental issues are being addressed within the lending program. Most agricultural and forestry loans now contain environmental components such as land and soil conservation, integrated pest management techniques, wildlife management, forest protection, and rehabilitation of drainage and irrigation systems. Almost all energy projects, where necessary, contain loan conditions to improve pricing of fuels and the efficiency of energy consumption, and many include environmental elements that deal with energy conservation, air and water pollution, and problems associated with dams and resettlement. This trend towards integration of environmental concerns into the Bank's operations will be further promoted by the emphasis on the environment which IDA donors have called for during the recent negotiations for its ninth replenishment.

Evolving Issues

The Bank is integrating the priorities identified by the environmental studies into its country economic, sector, and project work. Some 30 major environmental projects are expected to be approved by the Board of the Bank over the next three-year period; these span a variety of sectors, targeting such areas as integrated watershed development, resettlement, wildlife protection, natural resource conservation, and industrial energy conservation. Moreover, recently introduced environmental assessment procedures is helping to ensure that the environmental consequences of individual projects are examined at an early stage and needed remedial action incorporated into project design.

Although the Bank has rapidly succeeded in integrating environmental concerns into its operations through this multi-pronged approach, a number of unresolved and strategic issues remain to be dealt with. Resolution of these issues would facilitate the streamlining of

Box 2: Environment Strategy Study for Poland

Late 1988, at the request of the Government, the Bank initiated a study on environmental issues in Poland with a view to assisting the Polish authorities in the design of an environmental strategy for the country as part of the overall economic restructuring program.

During the first phase, completed in June 1989, the study identified air and water pollution as the most prevalent environmental concerns in Poland. The survey indicated that the severe degradation of Poland's environment can be attributed largely to systemic problems associated with central planning - industry's high share of national output combined with a bias towards heavy industry; high material and energy intensity of all industrial output; neglect of operation, maintenance, rehabilitation, and modernization; and a constant shortage of investment funds, especially for "non-productive" purposes such as pollution monitoring and abatement. It was also found that the greatest negative impact on the environment stems from Poland's extreme reliance on underpriced coal and lignite for primary energy consumption (75% as opposed to 24% in Western Europe as a whole). The resulting total annual cost of environmental degradation in Poland has been estimated to correspond to at least 10-15% of the national income. While, in principle, environmental legislation and regulations in Poland have many desirable characteristics (e.g. standards, impact statements, permits, user chargers, tax breaks), in practice the system is nullified by ineffective levels of fees and fines, ad hoc exemptions, and too strict standards combined with inadequate monitoring and enforcement capacity. Thus, the first phase concluded that substantial technical assistance and a suitable institutional and regulatory framework are required to prepare an investment program and manage the increasing offers of financial aid from various donors.

In addition to confirming the findings of the first phase, the main mission which visited Poland in September 1989 found that: (i) airborne pollutants threaten human health more than waterborne exposure; (ii) enforcement of the existing system of standards, fees, and fines can be considerably improved; (iii) linkage between monitoring, data analysis (including health and economic impacts), management decisions and regulatory actions could be greatly strengthened; (iv) present water resource investment strategies have been heavily influenced by the extensive water pollution in the Oder and Vistula basins, resulting in expensive "end-of-pipe" solutions and deferring pollution control at the source; and (v) more attention to solid and hazardous waste management is urgently needed. Moreover, in line with the conclusions of the first phase, the main mission identified an Environmental Management Project to address some of the major issues identified by the study.

The proposed Project, focussing on three of the officially designated "ecological disaster" areas (Katowice, Kracow and Legnica), would finance technical assistance and specialized monitoring equipment to: (i) strengthen environmental policy, regulation and program coordination, (ii) develop and implement a program of industrial efficiency and environmental reviews, (iii) improve air quality planning and management, and (iv) support the transition to a water resources planning and management system based on river basin authorities. This project, the first of a series to assist Poland in its environmental efforts, was appraised in December 1989 and implementation is expected to start in May 1990.

environmental priorities into the Bank's work. These issues can be summarized under two main headings: (i) conceptual and practical problems involved in bringing environmental management into the mainstream of economic policy making and (ii) what should be the Bank's role in the special problem of the "global commons". These issues are at the cross-roads of the Bank's future role and involvement in environmental activities.

Conceptual and Practical Problems. The Bank's traditional approach to project selection is based on an analysis of cost and benefits which are tangible and/or quantifiable. This approach is not useful in situations where complex environmental consequences are involved. In these situations, such standard valuation problems as the welfare of future generations, irreversible damage, and externalities are often exhibited to an extreme degree. It is increasingly recognized by the Bank that traditional analysis should be supplemented by an equally rigorous appraisal of physical and distributional effects. The Bank is carrying out work to establish guidelines which dictate how far the traditional cost-benefit approach can be used and where it needs to be supplemented by assessing nonmonetary impacts.

Furthermore, sound economic policies require a better understanding of the causes of environmental degradation, as well as the social and economic significance of the phenomenon. Determining causality, a necessary step in introducing remedial measures, is difficult because of the interdisciplinary nature of environmental questions, and the complex interactions between natural events and human activities. The Bank is working on these questions by investigating the usefulness of geographic information systems, including remote sensing.

There are four areas that in the near future will constitute the main focus of environmental action within the Bank's country economic, sector, and project work. These will include: (1) research into the extent to which national income accounts would be affected if environment is accounted for properly; (2) the extent to which environmental degradation threatens sustainable economic growth and country credit-worthiness; (3) establishing methodologies to assess priorities for environmental actions; and (4) the identification of economic policies to address environmental issues.

Global Commons. In its work with borrowers, the Bank also confronts environmental areas with significant global implications. A good example is in the field of energy efficiency and conservation which because of the increasing threat posed by global warming will become still more important in the future. Projects and programs which aim to improve the efficiency of power supply and end-use result in cost savings while at the same time reduce the amounts of greenhouse gas emissions. Examples include the FY88 and FY89 projects in Argentina, Bangladesh, India, Malawi, Morocco, Somalia, and Zimbabwe, all of which specifically address improvements in utility efficiency. This focus on the global environmental repercussions of its actions is playing an increasingly important role in shaping the character of the Bank's activities.

Institutions and Agencies Concerned With Global Environment Issues

Background Note No. 2

Introduction

This note reviews the principal bodies which governments have asked to deal with environmental activities with significant global implications. These activities address the major threats to the global commons arising from global warming, loss of biodiversity, degradation of international water resources, and depletion of the ozone layer. It is fully recognized that there are many other institutions and agencies active in these areas.

Global Warming

Following a meeting of agency heads in July 1988 it was agreed that the two lead institutions would be:

UNEP (United Nations Environment Program)

Set up following the Stockholm Conference in 1972, UNEP has a general mandate to act as a catalytic and coordinating agent within the U.N. system. It had early focussed on climate-related issues (e.g., desertification and ozone depletion in the late 1970's); more recently, the 1989 meeting of the Governing Council placed climate change and ozone depletion on a priority list of seven "areas of concentration".

WMO (World Meteorological Organization)

From the technical point of view, and as an agency equipped to evaluate the various models of global climate, WMO has the expertise to monitor overall trends and advise on the degree of threat, as well as areas of uncertainty.

The activities of UNEP and WMO led to the creation in late 1988 of the following:

IPCC (Intergovernmental Panel on Climate Change)

Governments have used this to organize their own dialogue on key aspects of climate change and assess possible responses. The main participants are developed countries and a number of specialist working groups have been set up. A first interim report on World Climate will be produced in mid-1990. 1/

ICSU (International Council of Scientific Unions)

Although strictly non-governmental ICSU has had an important role in attempting to coordinate the vast range of scientific activity undertaken nationally and internationally in recent years.

1/ A number of proposals for new bodies to deal with global climate factors have been made at various intergovernmental meetings but at this stage no formal moves have been made to establish any new agency.

UNESCO (United Nations Educational, Scientific and Cultural Organization)

Within its scientific brief, UNESCO also needs to maintain an active interest in the implications of climate change.

Loss of Biodiversity

As might be expected, the main impetus here has come from the scientific community, with an increasing accent by developed countries on the urgency of the situation, but little official endorsement (outside the NGO community) from more than a handful of developing countries. Some organizations and conventions concerned with biodiversity matters include:

IUCN (International Union for Conservation of Nature and Natural Resources)

This is an organization which groups scientific and conservation interests with governments in an unusual format. It has been the natural leader in a mounting campaign to protect endangered habitats and species. It prepared the World Conservation Strategy (WCS) in 1980 (together with UNEP and the World Wildlife Fund) and has drawn up a series of national conservation strategies, as well as advising directly on Bank projects. IUCN publishes the "Red Data Book" on the status of endangered species. A Second World Conservation Strategy is currently under preparation. IUCN is also actively promoting the concept of a "Biodiversity Convention" as a vehicle for international action.

CITES (Convention on International Trade in Endangered Species)

This convention attacks biodiversity from the "edge of the cliff", i.e., by erecting some barriers against extinction through the pressures of commercial trade. There is still a vast illegal trade, particularly in exotic birds, but CITES has succeeded in bringing the scientific evidence of declining population (e.g., of the African elephant) to a much wider audience. It is strongly supported on the information side by an NGO network (TRAFIC).

FAO (Food and Agriculture Organization)

Apart from being "associated" with the WCS, FAO's function in relation to tropical forests (it provides the secretariat for the Tropical Forestry Action Plan) brings it into a key aspect of global biodiversity.

UNESCO

Also "associated" with the WCS, it has an interest both in the scientific aspects as well as the "world heritage" area in its cultural brief. The World Heritage Convention, which UNESCO administers, covers both natural and human heritage.

UNEP

Has sponsored much of the international dialogue on biodiversity and has brought into relief the perspective of developing countries.

It is difficult to separate out the endeavors of the private conservation sector, that is the NGO's, the academic institutions, botanical gardens, zoos, etc. who bring large resources to bear. Sometimes they have been the trigger for new techniques, such as debt-for-nature swaps, as well as creating considerable publicity about the fate of individual species - largely through TV or specific fund-raising for one species which is at risk - the "panda syndrome".

International Water Resources

Hardly any international agency is not involved in some way with water, so the list could be very long indeed. Examples of some major actors include:

FAO - irrigation, groundwater, pesticide and other residues.

WHO - (World Health Organization) - clean water supply, safe sewage treatment, disposal of toxic and other wastes.

UNESCO - scientific data on trends in water quality.

UNIDO - (United Nations Industrial Development Organization) needs of industry, waste water treatment.

This could be expanded to include regional arrangements such as the Barcelona Convention, committing countries around the Mediterranean to have regard to impacts on that water body.

Of special importance at the global level are:

IMO (International Maritime Organization)

Aspects of marine transport affecting the oceans, oil spills, dumping (controlled under the London Dumping Convention), safety at sea, etc.

UNDP (United Nations Development Program)

As the technical assistance arm of the UN, UNDP has always devoted a large portion (currently around ___% of total flow) of assistance to water-related projects.

UNEP

Apart from keeping water on the global environmental agenda, UNEP launched the Regional Seas Program, which has produced action plans in the Mediterranean and throughout the world.

Ozone Layer

Here UNEP has been the lead agency, promoting the conclusion of the Vienna Convention for the Protection of the Ozone Layer (1985) and the Montreal Protocol (1987) to this Convention (see para. 33). UNEP provides the secretariat for the Protocol, as well as the political impetus for more rapid phase-out of CFC's and other harmful chemicals.

WMO, WHO, and other agencies are also active in the scientific study of trends in the ozone layer and health impacts. Major input has come from national research programs in Antarctica and elsewhere, particularly by the US.

Alternative Mechanisms for Financing Environmental Activities

Background Note No. 3

Introduction

During the time of the Development Committee meeting in Washington in September 1989, it was proposed that a variety of financing mechanisms should be explored that might facilitate financing environmental programs and projects. These proposals were not specific with respect to the type of financing mechanisms to be considered.

This background note is intended to provide an overview of the various funding mechanisms which might be used to finance environmental programs. It distinguishes the various mechanisms in terms of whether they are of the *traditional* type, having been used in development assistance before, or the *non-traditional* ones, which have been advanced more recently as new and innovative mechanisms, specifically aimed at meeting environmental concerns. The paper discusses the distinguishing characteristics of each funding mechanism. Some conclusions are then drawn as to their relative practicality in serving as a mechanism through which to provide funding to support environmental activities in developing countries.

Traditional Funding Mechanisms

There are essentially three main categories of funding mechanisms that classify as of the traditional type. These include:

Multilateral Assistance Programs. These programs combine the support from various sources into a unified development assistance framework. There are two traditional formats for this approach. The first is exemplified by the World Bank as well as the regional development banks. These institutions obtain their funding through capital subscriptions from members which provide the basis against which funds can be borrowed in the open markets for use in development. The second approach to multilateral funding is exemplified by IDA, a facility through which multilateral concessional development assistance is provided using funds obtained from donors on a voluntary basis but guided by the principle of burden sharing. The replenishment of funds is periodically needed since the concessional nature of the support does not generate sufficient reflows to support new activities. The funds for multilateral development assistance commonly derive from the multilateral aid budget of donors.

Bilateral Assistance Programs. This approach is often used by donors for the purpose of maintaining full control, involvement, and identification with the assistance being provided. Most major donors participating in international development assistance have their own agency responsible for funding activities on a bilateral basis. Examples of such agencies include the USAID, the Canadian CIDA, and the Swedish SIDA. Many donors provide bilateral development assistance through their foreign ministries. Bilateral support also takes the form of co-financing activities whereby donors will provide partial financing of activities which have been prepared by other (commonly multilateral) development agencies. In this way, the donor benefits from the technical expertise and input of the coordinating agency while still maintaining full control of the specific activities for which its funds are used. Another mechanism which falls under the bilateral funding category is the **Trust Fund**, of which the Technical Assistance Grant Program for the Environment is a recent example. Trust Funds are facilities administered by established institutions, such as the World Bank, which are legally separate from the operations of the institution. They are usually established to address a unique funding objective -- for example technical assistance for project preparation -- and can receive contributions with a specific mandate. They are usually supported by grant contributions from specific bilateral sources.

Programs combining bilateral and multilateral support. These programs combine multilateral and bilateral assistance into a coordinated funding mechanism. The Special Program for Africa (SPA) and the Special Joint Financing (SJF) channel of the Special Facility for Africa (SFA) are examples of such a program. In these cases, the World Bank, IDA, or other multilateral agency (e.g. the UNDP) would administer the funds and contribute to the core program. This core program would be supported by bilateral funds. Bilateral donors, however, would retain control over specific operations they wish to fund. These programs allow donors to ensure mutually coordinated action in an area of common interests and objectives.

Non-Traditional Funding Mechanisms

Several innovative funding mechanisms have been proposed recently within the context of discussions on the need for action on the environmental front. These include mechanisms by which resources could be mobilized for environmental activities, but also mechanisms by which available resources can be effectively channeled to collective objectives. The non-traditional funding mechanisms which have been proposed, most of which can be classified as being either of a voluntary or assessed nature, include:

A Carbon Tax Initiative. This mechanism is based on the principle that the polluter should pay. It requires international agreement and participation, since punitive taxes are levied on the basis of a country's emission of greenhouse gasses, measured in terms of the impact of the emitted gasses on global warming. Such an initiative would lead to a reduction in the amount of fossil fuels used (and thus greenhouse gasses released) while simultaneously raising revenues for use in other environmental activities. This proposal is controversial both because of the as yet limited scientific evidence on the connection between greenhouse gasses and global warming, as well as the effect of such a tax in reducing consumption. In addition, the international political controversies in terms of verification and fairness that such a mechanism would generate can be expected to be immense. And, history shows that assessed contributions are not always reliable, with countries paying late or withdrawing support if they do not agree with the perceived spending policy.

A Clearinghouse Fund. This type of mechanism is based on the premise that, from a global perspective, it may be economically more efficient for some countries to subsidize activities in other countries which result in reduced atmospheric greenhouse gas contents than to curtail greenhouse gas emissions domestically. In other words, the clearinghouse approach enables action of one country to be substituted for by more efficient action of other countries. The concept is one of maximizing, on a global scale, the marginal impact of funding curtailment of greenhouse gas emissions and would work as follows: Assume that the curtailment by an industrialized country of its greenhouse gasses by x units would cost $100 million. And assume that by planting $50 million of tropical forests in a developing country instead, the same x amount of greenhouse gasses could be absorbed. Clearly, from a global perspective, the latter would be the most economical approach. The clearinghouse mechanism would be to raise funds by (voluntary) contributions from the industrialized country and use them in the developing country. Expanding this mechanism to include most countries into a global clearinghouse system is the ultimate objective of the proposal.

Levies on Trade. This mechanism has been proposed particularly in the context of efforts to protect bio-diversity. It comprises levying, for example, a 1% import tax, to be paid by consumers in developed countries and collected at the port of entry on imports of commodities originating from areas in tropical climates, characterized by high bio-diversity. Analysis shows that the 1% tax would have virtually no impact on consumption, and thus would not affect the trade balances between the countries but would result in substantial amounts of funds raised. This approach could be extended to the trade in logs or other forest products.

A Private Sector Facility. The premise for such a facility is that intermediation similar to that provided by investment banks could lead to mobilization of long-term capital, spread-risks, arrange access to technology, and improve incentives for investments in sustainable resource management. By demonstrating that well conceived projects that use natural resources sustainably can generate significant returns to investors, private investment can be mobilized in much greater volumes than the facility finances directly. Examples of the kind of activities include: Wildlife Utilization, Sustainable Forest Management, Renewable Energy and Energy Conservation, Eco-tourism, Sustainable Mariculture.

A Burden-sharing Environmental Levy. This mechanism, involves a contribution from all countries based on a percentage of GNP. 0.1% of GNP has been proposed, to be subscribed to by both developing and industrialized countries. It is estimated that some US$ 18 billion could be raised in this fashion. Other proposals along this line also include a contribution of 0.1% of GDP, but only from donor countries. Since these programs are of the 'assessed' type, the problems associated with compliance and participation, already mentioned, are likely to arise.

Diversion from other Funds. This mechanism relies on the earmarking of funds or the outright transfer of funds already allocated to other development assistance for use on environmental activities. For example, one specific proposal called for the allocation of about 3% of IDA to be used on technical assistance for environmental activities. This mechanism would eliminate the additionality factor in mobilizing funds for the environment. Since development assistance now integrates significant environmental components and aspects into its program, the net effect on the environment from such diversion of funds would be minimal.

Royalties. Proposed in the context of funding mechanisms for bio-diversity, this approach relies on earnings from new products or intellectual property derived from bio-diversity. It is not clear how this approach could be extended to other global environmental objectives. Even in the case of bio-diversity, its practicability is questionable.

Private/Non-governmental contributions. NGOs have increasingly shown material interest in providing financial support for the environment. However, these contributions, on a world-wide scale, and in proportion to the magnitude of the needs as perceived, are rather small. In the particular area of nature conservation however, NGO financial contributions have been quite significant. Debt-for-Nature swaps have provided a useful way of leveraging NGO contributions in certain cases.

Contributions in Kind. These would include voluntary in-kind contributions to support environmental objectives. For example, governments might designate park lands, monitoring operations, or cleaner technologies for energy and industry.

Lotteries and Other Fund Raisers. These could include a tax on tickets at big international events such as the Olympics or World Cup Soccer, World's Fair events, etc., as well as similar national-type of events. In addition, fund raisers for the environment, like telethons would potentially also yield considerable contributions. In addition, it has been proposed that an international Environment World Fund lottery be organized as a means mobilizing collective private contributions.

Issues and Conclusions

As a general rule, the main advantage of the traditional funding mechanisms in contrast to the non-traditional ones is their proven viability and donor familiarity with them. Some of the non-traditional mechanisms proposed may indeed eventually lead to substantial additional mobilization of financial resources for the environment. However, these approaches represent a significant departure from past practices and many of them raise serious questions as to the practicability of their implementation. There is therefore considerable question as to how quickly international political support for them could be mobilized into action. In all likelihood, considerable time will need to be expended on defining and agreeing on the detailed modalities of these new mechanisms.

In view of the urgency expressed by donors as well as developing country representatives as to the need for immediate action to address environmental policy and programs in developing countries, a more conventional mechanism as an initial step would be recommended. Clearly, it would not have to be simply one of the three traditional mechanisms outlined above. Instead, it could combine the best features of each and thus provide a mechanism which can respond quickly and flexibly to the various needs which encompass environmental support in developing countries. The choice as to what mechanism to adopt for the eventual creation of an environmental fund remains an important issue to be resolved.

Mr. OBEY. Thank you very much.
Mr. Wright?

MR. WRIGHT'S OPENING STATEMENT

Mr. WRIGHT. Thank you. I appreciate being here this morning.

As you have heard, there are a range of issues that this country confronts around the world. Similarily there are a wide range of steps that need to be taken by the U.S. Government to maintain or reassert a leadership position on global environmental concerns, as on concerns with poverty, and on the linkage between these two issues.

The World Wildlife Fund, which I represent, believes that foreign assistance is the most direct and the most immediate way for the U.S. to express its concern over environmental and poverty issues and to attack these problems.

We have had the opportunity to observe A.I.D.'s performance under the Congressional biological diversity earmark.

We have worked with the Central Bureaus of A.I.D.—Science and Technology, Office of Private Voluntary Cooperation; we have worked with the regional bureaus and we have worked with individual missions.

WWF runs 400 to 500 projects around the world and has had a chance to deal with A.I.D. as colleagues in the Third World struggling with the same realities. I'm sure A.I.D. will document on how hard it is to make the conservation-development link work in the field.

Overall A.I.D.'s performance has been remarkably good. I think Congress should feel that its directives have been heard.

With the first round of earmarks on biological diversity, there was some real reluctance on A.I.D.'s part. The initial reaction of A.I.D. was "this, too, shall pass". They tried to fund everything on a one-year basis on the assumption there wouldn't be an earmark in the future.

One thing that we have found, when you work in the environmental field, as when you work in poverty, you have to make a long term commitment.

It's not the kind of thing that you do on a one shot basis in one year and hope it goes away. It's terribly important that both A.I.D. and Congress maintain a long term commitment to this issue if we're really at all serious. Very often the amount of money is less important than how long you're willing to stick with a project or program. But A.I.D. has now passed that initial point where they felt biodiversity was something that would go away and have begun to internalize the process.

My colleague from The Nature Conservancy will talk more about Latin America, so I will focus on A.I.D.'s performance in Africa and Asia.

A.I.D.'S BIODIVERSITY PERFORMANCE IN AFRICA AND ASIA

In Africa, the primary mechanism that A.I.D. has used on biological diversity has been implementation through the U.S. nongovernmental community. They have tended to act to some extent like a grant maker. A.I.D. has asked the environmental community to come forward with proposals. These groups are in touch with Third World governments and NGOs and have become the implementing arm of A.I.D. in Africa.

It's led to some very good and creative projects. Certainly, given staff limitations, this is a fairly creative way of moving into a new area of activity.

It does have a drawback, however. It tends to leave A.I.D. out of projects that have long term institutional support, and one of the greatest weaknesses of environmental programs in Africa is long term commitment to African institutions. We need to begin to build up the base of competent and trained individuals through local institutions. So while I applaud the use of NGOs as an implementing mechanism, there are limits to that mechanism as well.

The elephant earmark that came forward last year was even more specific than biological diversity. It caused a lot of shuffling feet and concern, but in the end, A.I.D. did the right thing. They focused A.I.D. elephant funding primarily on habitat conservation and institution building. They have looked at a number of National parks and have begun to put funds into increased protection. They have left the Fish and Wildlife Service to focus on ivory trade and enforcement/customs issues in dealing with the elephant crisis.

It seems to me that's a sensible division of responsibility with Fish and Wildlife and A.I.D., each doing different things. Up until now, however, it has not been a formalized division of responsibility. It would be good if A.I.D. and FWS talked together and developed a more coherent and formal strategy to deal with elephants.

Asia is a rather different situation. In my opinion the Asia environmental staff is the best in the agency. There really are some superb individuals, both at the central office and in the field, and there's a lot of interest within Asia itself both with the governments and NGOs.

If there is any place that A.I.D. has a chance to make a real mark in the area of conservation and development, to provide real leadership, it is in Asia.

We've been very enthusiastic about ~~some~~ of the initiatives started in Asia, and yet this is the place where we have to raise the greatest concern and alarm.

What we are hearing from our Thai colleagues is a real sense of discomfort with A.I.D. These colleagues feeling that A.I.D. has made commitments in Thailand for a very ambitious program known as RENARM and suddenly, after several years of delicate negotiations, there seems to have been a whole new set of ground rules being applied by A.I.D.

The new rule is a thing that is called "an economic filter" although it's gone by different names. Suddenly everybody has to jump through a set of hoops that they didn't have to jump through before.

Obviously, our concern is that economic issues get addressed along with environmental; A.I.D. has supported this, and we have supported it. We have a program called Wildlands and Human Needs that looks directly at the link between human welfare and environment, so I have no problem with A.I.D. trying to bring the issues of economics and environment together.

But to come in with essentially an economic gate that you've got to go through before you can deal with environmental issues and to imply that A.I.D. should support a country's economic path whether it's sustainable or not, just simply makes no sense.

It's terribly important that this committee make clear to A.I.D. that these sorts of qualifiers and criteria being applied to earmarks after the fact is simply not acceptable.

WWF is fairly sympathetic with A.I.D. and its desire not to be micromanaged and not to be earmarked to death. On the other hand, you look at the Philippines where, at first, A.I.D. seemed to be waffling on the environmental conditions. When Congress came in and was absolutely unequivocal that environment was part of the dynamic that had to be addressed in the Philippines. A.I.D.'s performance has been quite good, given the political situation.

So I would challenge my colleagues in A.I.D. with the Philippines example and the Thailand example and say, "look, you say you don't want to be earmarked. On the other hand, in the Philippines, when Congress came in and told you how to do your job, you did it; in Thailand Congress gave you a little running room, and suddenly you've got a whole different set of rules."

This new criteria is not just applied to Thailand. We're hearing the question of what will they do next in India and Indonesia? There's a lot of project design going on out there, and people don't understand now whether or not biological diversity is still a priority or is it something you do after everything else is taken care of?

There's a second aspect of the Thai example that is important and which also applies to Latin America. Where does environment and biological diversity fit in the countries that begin to move out of traditional A.I.D. support, as they become more advanced developing countries?

Some of the most important biological countries in the world, Mexico, Colombia, Brazil, potentially Thailand, could move into this status. It is important in those countries with strong environmental institutions and important global biological resources that biological diversity remain a priority as A.I.D. develops new strategies reflecting their evolving economic status.

At the moment, the global warming initiative is providing the window to allow a lot of biological activities to be undertaken, particularly in Latin America and other advanced developing countries.

A.I.D. PROBLEMS IN BIOLOGICAL DIVERSITY

There are a couple of general issues on A.I.D. performance under biological diversity which apply to the agency as a whole.

The first, which was mentioned by my colleague earlier, is environmental staff. You need technically trained staff. These aren't the kinds of things you can do only with generalists.

We would like to see additional staff. I testified before the A.I.D. Advisory Committee on Voluntary Foreign Assistance, and the A.I.D. coordinator said there was a commitment to hire 100 new environmental staff.

There was sort of a gasp, but we checked the figure, and it was 100. I would like to hear from the Administration whether this figure is a commitment that A.I.D. is prepared to live up to and when they're going to start the process.

A second problem, even with existing A.I.D. staff, is rotation; the problem of staff moving around. It's very difficult to maintain long term relationships on natural resource issues if your staff is leaving every 12 to 24 months.

One of the best missions I've dealt with is in Zambia, but all the key people now have left, and we are back to ground zero in terms of project awareness.

One solution is to look more to locally hired professionals. There are some very good local hires, such as there are some excellent staff in the Zimbabwe mission.

While building continuity, by bringing local hires you also start expanding the base of local environmentalists.

A.I.D. can be creative; it's not just a matter of saying we can't do these things. If we really think about it, there are solutions to many of these problems.

Another staffing issue relates to the World Bank, A.I.D.'s "early warning system." A.I.D. has only one full time person trying to monitor the environmental performance of the World Bank.

That's just ludicrous. It can't be done by one person. We applaud the fact that A.I.D. is trying to monitor the Bank's performance, but they've really got to be serious. I would hate to talk to the spouse of the individual involved.

The final point I'd like to make is the question of oversight versus micromanagement. As I observed, A.I.D., has done a reasonably good job on biological diversity, but it's terribly important that there be accountability at the top.

This committee cannot reach around and try to tell a project officer in Zimbabwe or in Bolivia or in Nepal how to do his or her job there. Somehow the Committee needs to make clear to the people at the top that they have a responsibility for the people who work for them.

I was disturbed by the Administrator's answer to some of the questions when he testified at his confirmation hearings. He indicated he didn't think appropriate by fiat from the top to tell people what to do. He felt somehow leadership should trickle down. I just think that doesn't wash.

The strongest environmental record of A.I.D. was during Peter McPherson's period in leadership. He made his personal commitment very clear and unequivocal, and people in the field knew it.

Without that commitment from the Administrator, the message is going to have to come from somebody else, and it may have to come from Congress.

So I would put the ball in A.I.D.'s court to establish whether they are serious about biological diversity leadership. Thank you.

[The prepared statement of Mr. Wright follows:]

WWF

World Wildlife Fund

Conservation of Biological Diversity
U.S. Action Through Foreign Assistance

Statement of R. Michael Wright
Vice President for Sustainable Development
World Wildlife Fund

Before the

Subcommittee on Foreign Operations
Export Financing and Related Programs
Committee on Appropriations

April 3, 1990

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Affiliated with The Conservation Foundation

World Wildlife Fund is the leading private conservation organization working worldwide for the conservation of nature. World Wildlife Fund is a field-oriented organization, supporting individuals and institutions that carry out practical conservation projects on the ground. Our highest priority is conservation of tropical forests, wetlands and other biological resources in Latin America, Asia, and Africa, places that are home to a substantial proportion of the world's animal and plant species. Founded in 1961, WWF has worked in more than 100 countries to sponsor and carry out over 1,600 projects involving a comprehensive array of conservation methods. WWF now has over 800,000 members in the United States. Altogether, the WWF family of 27 national organizations has 4 million supporters around the world.

Conservation of Biological Diversity
U.S. Action Through Foreign Assistance

Statement of R. Michael Wright
Vice President for Sustainable Development
World Wildlife Fund

April 3, 1990

Mr. Chairman, Members of the Subcommittee, thank you for this opportunity to present the testimony of World Wildlife Fund on the U.S. Agency for International Development's (A.I.D.'s) biological diversity program.

I do not think it necessary to spend a great deal of time outlining the importance of preserving biological diversity. The ongoing destruction of the world's plant and animal species is well documented: 100 acres of tropical forests disappearing every minute and an extinction rate 400 times higher than that of the recent geologic past are just two disturbing indicators. Less well recognized is the link between loss of biological diversity and human poverty. The destruction of the natural resource base upon which the poor depend, the majority of whom are poor women, is irrevocable and accelerating around the world.

The question is not whether biological diversity is becoming threatened nor whether the survival of the world's poor is at stake, but how the United States can best respond to the threat that exists. There are a number of paths that must be pursued, ranging from debt relief to GATT regulations which make the best environmental technologies available to the third world at reasonable cost, but WWF believes that the most direct, effective short-term answer lies in foreign assistance. No other program provides the type of immediate, on-the-ground resources for protecting critical ecosystems and species; no other program provides for the integration of human needs with biological conservation.

Congress recognized this when it instructed A.I.D. to develop a program to conserve biological diversity as part of its development mandate and earmarked funds for this purpose. WWF has been a strong supporter of these biodiversity earmarks. In light of the vigorous internal competition for funds among A.I.D.'s priorities, environmental concerns would have had great difficulty in vying for major support within the Agency without the attention and earmarks that Congress has provided.

The question I will address, then, is: How is A.I.D. doing?

Program Overview

WWF has worked closely with the Agency in implementing its environmental programs. During this past year alone, for example, WWF undertook approximately 500 projects in the developing world, some 300 in Latin America and the rest divided more or less equally between Africa and Asia. A number of our programs received A.I.D. support or were carried out in partnership with the Agency, giving us ample opportunity to observe the Agency in action and to evaluate its implementation of the directives of the Congress.

Our experience has been, for the most part, positive. The A.I.D. staff with whom I have personally worked are dedicated professionals, both in the central bureaus and in missions such as those of Thailand, Zambia and Bolivia.

A.I.D.'s support for initiatives in the areas of tropical forest management, conservation of biological diversity, and ecologically sound development has been important in allowing WWF to move aggressively into areas of basic human needs linked to conservation of natural resources. For example, A.I.D.'s Office of Science and Technology has created the Biological Diversity Support Program, a joint venture of WWF, TNC and WRI which provides technical assistance, training, information for A.I.D. missions on conservation activities, and also funds small grants and pilot demonstration projects on biodiversity conservation such as protected area management in Nepal and Madagascar. The Office of Private and Voluntary Cooperation supports several biodiversity-oriented programs, including WWF's 5-year Wildlands and Human Needs Program, which now runs more than twenty projects around the world designed to promote local economic growth while protecting biological resources. Just one example in the Central African Republic links health care for the local pygmes with establishment of a multiple-use protected area to protect forest elephants. A.I.D. support, combined with WWF funds, has also made possible debt-for-nature swaps in Madagascar and the Philippines. WWF strongly encourages A.I.D.'s continued use of innovative conservation financing mechanisms like debt-for-nature swaps, local or counterpart currency accounts, and endowments.

A.I.D. employs rather different biodiversity strategies in Latin America, Asia, and Africa. Geoff Barnard of The Nature Conservancy is describing Latin America, I will highlight Africa and Asia.

Africa

In Africa, A.I.D.'s biodiversity efforts focus on protected area management and have been, for the most part, a success. The Africa bureau has relied heavily on the NGO community to carry out its program through support to NGO conservation projects such as Wildlife Conservation International's work to preserve biologically rich Korup National Park in Cameroon and a joint WWF/CARE project supporting area protection and buffer zone development in Uganda's Impenetrable Forest, home to the endangered mountain gorilla and other unique species. A.I.D. is also exploring involvement in biological diversity projects in The Gambia and Guinea Bissau in West Africa, and has strongly supported a community-based Resource Utilization Project involving Zambia, Zimbabwe and Botswana.

A.I.D.'s strategy of working closely with NGOs in implementing its African environmental programs has much to recommend it. For one thing, the lack of environmental field personnel in Africa (an issue I will describe in detail later) makes cooperation with conservation groups imperative. Partly through such cooperation, the Africa bureau has managed to develop a number of projects that go far beyond mere compliance with Congressional directives. We do, however, have concerns about the lack of environmental staff in the bureau, and worry that the Agency's reliance on NGO partners could allow A.I.D. to meet its biological diversity mandate without actually institutionalizing concern for the issue.

Along with these general biological diversity projects, A.I.D. engaged in a concerted campaign to prevent the extinction of the African elephant. WWF strongly supported last year's congressional earmark of $2 million for USAID to implement elephant protection programs, and believe this money should go to projects which reflect the Agency's strengths: 1) financing institution-building for African park and wildlife departments, as it has done in Tanzania, where AID is spending $2.5 million in FY 1990 to train Tanzanian parks and wildlife personnel in the development of land-use management plans; 2) funding specific field actions like its $250,000 project to develop an elephant management plan for Park "W", Niger; and 3) sponsoring public awareness programs aimed at fostering support for elephant conservation among local human populations in Africa, such as its extension work in the communities surrounding Tsavo National Park and Masai Mara National Preserve, Kenya, which cost $300,000 in FY 1990; and 4) developing programs to link wildlife conservation with community development similar to the Zambia Wildlands and Human Needs Program, which recieved $2.8 million in FY 1990.

Support for such activities has been outlined in A.I.D.'s plan for meeting the earmark, and WWF is encouraged by the initial direction of the Agency's. We believe it is critical for the Agency to sustain its efforts, and therefore are urging Congress to earmark $5 million for A.I.D. to meet its obligations in fiscal year 1991. WWF will continue to closely monitor A.I.D.'s progress, as I am sure will the Congress.

Asia

The quality of environmental staff in the Asia and Near East region, combined with capable and interested local institutions, gives the region great potential for a cooperative A.I.D.-host country biological diversity program of major importance.

WWF is therefore very disturbed to see the Asia regional program begin to lose momentum over an issue that many in the environmental community had thought was resolved long ago: the need to justify long-term environment concerns by narrow, short-term economic and political criteria. It is our understanding that the Asia bureau has introduced a new set of conditions, referred to as a "filter," which qualifies and can in some cases conflict with the mandates established by Congress in sections 117, 118 and 119 of the Foreign Assistance Act.

I would like to present the case of Thailand as an example of the application of this "filter." Because the merit of projects is now being judged based solely on their contributions to economic growth, activities such as biodiversity research have been frozen despite applications made over a year ago by Thai universities and government agencies. The hold on environmental projects has been applied not only to future projects but also to ongoing commitments such as the MANRES (Management of Natural Resources and Environmental for Sustainable Development) project while a new A.I.D. design team subjects the various components of a previously agreed program to this new criteria. MANRES is an important seven-year integrated project including coastal, industrial and rural resource management, strengthening capability to manage biological resources, policy analysis and environmental educations.

WWF believes that A.I.D.'s actions have seriously jeopardized our relationship with the Thais, set back biological diversity conservation in a key country and damaged A.I.D.'s credibility. The approach being taken ignores the reality that project design and implementation of an effort as complex as MANRES requires ongoing discussions over several years, development of trust and reliance and cannot be arbitrarily turned on and off on political whim. The repercussions of the Thailand decision has created uncertainty throughout the ANE region, from India to the South Pacific, and the filter is distorting the design process of a major natural resource project proposed for Indonesia, one of the biologically diverse and critical nations in the world.

Further, WWF believes strongly that economic growth per se is not the only goal of foreign assistance. A.I.D. is a development assistance agency, and issues of quality of life and maintenance of a sustainable resource base are equally valid, not secondary, considerations. National economic criteria or filters mask the key role biological diversity plays among the poor, especially in rural areas. Projects which merely reinforce existing economic and resource inequities will not meet the needs of the poor who are the very ones now forced to destroy biological resources to survive. If a country's existing "economic path" is biologically unsustainable, it is hardly sensible to insist all projects promote it rather than alternative development approaches. To make quantitative economic growth, and growth alone, the arbitrary and subjective guideline by which all projects are judged is to put A.I.D. back ten years in its thinking at a time when the World Bank and others in the development community are acknowledging the disastrous projects which resulted from such single purpose approaches. We should not return to the era where "we knew the price of everything and the value of nothing."

WWF urges Congress to make clear to the Agency that the use of an economic "filter" to judge the merits of environmental programs and projects is unacceptable. Clear instructions, such as those provided in last year's Multilateral Assistance Initiative for the Philippines, would establish once and for that the environment and conservation of biological diversity is indeed a regional priority. I note that on the Philippines MAI, A.I.D. appeared at first to be ducking its environmental responsibility; however, since unequivocal Congressional direction was given, the program has proceeded as smoothly as local politics will allow.

Thus, WWF's experience with A.I.D. in Africa and Asia reveals that the effectiveness of the Agency's implementation of its mandate to protect biological diversity has depended to a large extent on priority placed on the issue by regional bureaus and mission staff. Where biodiversity conservation is embraced, a bureau or mission can be very effective. When resisted, progress in establishing environmental priorities and programs is slow and painful indeed.

From that regional perspective, I would now like to turn to some observations that WWF has made about institutional and structural hindrances to A.I.D.'s biodiversity program. WWF's work with A.I.D. has revealed general areas in which the Agency could improve its performance as an institution in conserving biological diversity, protecting the environment and meeting the needs of rural poor.

Specifically, we see the need for improvements in the following areas:

Environmental Staff

This past year Congress instructed A.I.D. to increase the number and expertise of personnel devoted to environmental concerns, including biological diversity, in its missions and bureaus. WWF applauded this language, as it is clear that A.I.D.'s ability to meet its biological diversity obligations hinges on the availability of technically trained professional staff. We were pleased, therefore, when in recent testimony before the U.S. Advisory Committee on Voluntary Foreign Assistance, A.I.D.'s environmental coordinator indicated there was a plan for hiring 100 new environmental specialists within the agency. However, we have not seen any action and would like to know if this is indeed an agency commitment, and if so, where and when would this process will begin.

An example of our concern over the environmental staffing situation in the Agency is the state of the "Early Warning System," the office established within A.I.D. to monitor the impact of proposed multilateral development bank projects on the environment and advise other agencies of its findings. Currently, the central office of the System consists of one full-time staff member with temporary assistance from an assistant assigned on a Fellowship from the American Academy for the Advancement of Science. This office is expected to coordinate the monitoring of hundreds of projects, and its staff are responsible for everything from interpreting project information to the clerical work involved in compiling and distributing reports (there is no support staff). The enormous task of following up on hundreds of projects simply cannot be accomplished by such a small staff, not because of a lack of dedication but because of lack of resources. Further, it is my understanding that unless renewed, the System's authorization expires at the end of the year. WWF urges Congress to renew the System's authorization. We also would strongly recommend that the System be given adequate staff resources by A.I.D., which we feel at a minimum would require one full-time staff officer for each region.

At the mission level, WWF would recommend that the Agency look to hire local personnel as a way of increasing the number and expertise of missions in the field of biological diversity and natural resource conservation. I understand there are excellent local natural resource managers in missions such as Haiti, the Dominican Republic and Zimbabwe, to name just a few. These locally hired professionals not only strengthen the missions, they create a growing professional cadre of local environmentalists and provide continuity as U.S. personnel move in and out of posts.

Personnel Rotation

Along with the lack of staff, another hindrance to A.I.D.'s ability to carry out its biological diversity mandate stems from the agency's personnel system. At present, staff in missions may rotate to different countries as often as every two years. Because of this process, missions lack continuity in many instances. All too often, projects initiated by one set of personnel are not considered commitments by subsequent directors or staff. If biodiversity projects are designed as they should be, based on long pains-taking local participation, abrupt shifts in direction can be devastating. Understanding of complex social problems which are the root causes of biological destruction is lost with each rotation.

In a new area such as biological diversity, staff turnover can have the advantage of making the Agency more responsive to new concepts. However, the need in the environmental and local development field for long-term project support and commitment to institution-building argues strongly for consistency and continuity. In addition, the rotation system can lead to domination by individual persons, with political or ideological concerns taking precedent over institutional policies, as some fear is currently happening in Asia. This approach can make A.I.D. an unreliable ally in a business where local trust may be as important as available financial resources.

Role of NGOs

A third problem affecting A.I.D.'s ability to fund activities to conserve biological diversity lies in the Agency's procedures for designing and implementing projects which too often effectively excludes participation by local and international non-governmental organizations. In some areas such as Africa, the Agency has done a good job of seeking out and consulting non-governmental partners in project design. Yet that approach is not yet institution-wide. In many regions, at the design level we are beginning to see a tendency to develop environmental projects through consulting firms and then ask NGOs to "bid" on them. NGOs may have only a peripheral role in the design and planning of activities, but are asked to act as contractors to carry out the work in question and report to the Agency.

WWF believes that U.S. foreign assistance in this arena would be far more effective if NGOs, in coordination with local people, participated in project design from the very start as partners, rather than contractors, for the Agency. The primary funding mechanism for project implementation should be an OPG (operating program grant) or cooperative agreement where A.I.D. collaborates with the NGO's own program activities rather than having NGO's act as an A.I.D. contractor, becoming merely an extension of the mission itself.

The urgency of the biological crisis tempts short-cuts in project design but solutions identified without local participation fostered by NGOs will be off-target and projects that neglect self-reliance will ultimately be unsustainable. If the biological diversity earmark is to be successful both we and Congress need to insist that A.I.D. engage in such a participatory process and in turn give A.I.D. the time needed to do so.

Small Versus Big Grants

WWF would also recommend that A.I.D. revise its procedures to significantly relax regulations and requirements on certain types of small NGO and PVO-related grants. Currently grants of $100,000 or $250,000 are regulated under the same requirements as much larger A.I.D. programs expending millions of dollars. Because most local conservation groups in developing nations lack the administrative capacity and staff to meet the Agency's reporting requirements, A.I.D.'s system for dispersing funds effectively excludes many of the small, grassroots groups that have proved critical to conservation.

ADC Strategy

Another growing challenge for the biodiversity earmark is its application in advanced developing countries (ADC). The need to develop such a strategy in Thailand has been cited as an excuse for holding up and redesigning of the MANRES project. An ADC strategy that looks only to U.S. short-term economic interests and ignores the global importance of biological diversity and the role in economic stability of sustainable resource management would be short-sighted indeed. This is no minor concern as some of the biologically most significant countries are ADC countries, including Thailand, Brazil, Mexico and Colombia. We would urge that Congress make clear, as it did on global warming, that biodiversity activities should be part of these country strategies. Given limited A.I.D. presence in ADCs, biodiversity concerns should be addressed through larger scale, institution building projects requiring minimal A.I.D. oversite and appropriate to ADC capabilities.

Accountability: Environment as an Institutional Priority

A final difficulty the agency has in implementing congressional directives on biological diversity and the environment is the apparent lack of effective accountability of senior management. WWF is concerned that there is a sense in the Agency that environmental priorities should "trickle down" from senior management rather than be mandated. The newly confirmed Administrator stated this opinion clearly at his recent confirmation hearings before the Senate Committee on Foreign Relations when asked how he planned to implement Congress' directive to sensitize A.I.D. missions and bureaus to environmental concerns.

WWF believes that leadership and priorities for the environment and conservation of biological diversity must come from the top, and Congressional directives should be targeted specifically for the top. We have seen this approach work very effectively in the past. On occasion, however, Congress has attempted to reach around the Administrator and assistant administrators, choosing instead to direct field staff through project earmarks and relying on ever more reports to Congress. These earmarks are a paradox. If they are too specific, they can remove the ability of bureaus and missions to work with local governments and NGOs in designing appropriate projects, and blur the lines of responsibility in the Agency. On the other hand, such earmarks have been critical in opening the Agency to the central role of environment in its development mandate, and have certainly been effective in focusing the Agency's attention and resources on critical issues such as biological diversity and elephant conservation.

The question is whether it is now possible to look beyond project level earmarks. If accountability can be established to avoid future Thailands, then perhaps environment should join rural development, agriculture, education, health and population as an institutional priority with a portion of A.I.D.'s budget clearly dedicated for the purpose. With the biological diversity initiative well underway, Congress should consider moving beyond the earmark to establish an Environment and Natural Resource 150 Account in the range of $150-200m for FY 1991. However, if this step is taken, performance should be monitored by Congress, as it surely will be by the NGO community.

Conclusion

WWF deeply appreciates the attention this Subcommittee has paid the environment and conservation of biological diversity in recent years. Through earmarks and instructions to A.I.D., the Subcommittee has helped foster both awareness and action to protect the earth's natural resource base. Yet work remains to be done:

1. Increased Staff

While essential, funding alone cannot make an impact on environmental concerns or poverty in the Third World unless coupled with knowledgeable, culturally sensitive staff able to listen to and work with people at the grassroots level. WWF recommends that Congress work with A.I.D. to develop and implement a concrete plan to increase the number of professional environmental staff in the Agency.

2. NGO Participation in Project Design

Inclusion of local NGOs and communities in the initial design of programs and projects is essential. Also, A.I.D. must recognize that many of these groups lack the administrative resources and expertise to meet strict reporting requirements. Their success depends on flexibility to respond to changing local conditions and needs. WWF would recommend that Congress work with A.I.D. to review their system for designing projects and dispersing funds to better include local NGOs.

3. Strong Leadership

A.I.D.'s commitment to conservation of biological diversity must come from the top of the Agency. Mission directors and staff do play a vital role in carrying out the mandates of the Agency, but without clear guidance from the highest levels, their efforts cannot ultimately achieve the best possible results amid a myriad of demands. This leadership should be clearly and directly responsible and accountable for implementation of Congressional earmarks.

In summary, most of the points made here are generic to the Agency as a whole, and the shortcomings mentioned frustrate its ability to meet its developmental as well as environmental mandates. While they certainly need Congressional attention, our conclusion is that A.I.D. as a whole is acting with growing commitment and creativity in the area of biological diversity. Congress should feel its earmark has had its desired effect in introducing a rather new set of concerns to A.I.D., and Congress and A.I.D. together should now seek to design mechanisms that will institutionalize these issues within the Agency.

Mr. **Obey**. Thank you very much.

Mr. Barnard?

Mr. Barnard's Opening Statement

Mr. **Barnard**. Mr. Chairman, on behalf of The Nature Conservancy and our new President, Mr. John Sawhill. I want to thank you for your attention to the issue of biodiversity. Echoing Senator Nelson, I want to underscore that biodiversity is not some esoteric terminology for scientists. In simplest terms, it is our global savings account, pool of genetic wealth, that someday we need to draw upon. It's really our ultimate safety net.

In Latin America, which contains approximately 60 percent of the world's remaining tropical forests, deforestation is now widely seen as a threat to the social, economic and environmental stability of the hemisphere.

We at The Nature Conservancy, and I know we share this with our colleagues at the World Wildlife Fund, feel that we must provide the tools to the people and governments of sovereign nations in Latin America so that they are equipped to protect their own environment within the context of a sustainable economic system.

I want to cover three points today. The first is an update on the Parks in Peril Program, which the committee supported in last year's appropriation.

The second are some comments on debt for nature swaps, including a key area of bilateral debt. The third are some additional comments on A.I.D.'s performance in Latin America.

PARKS IN PERIL PROGRAM

Last year, through the leadership of this subcommittee, The Nature Conservancy launched the Parks in Peril Program which will help protect 200 key biological sites, over 100 million acres of tropical habitats, by the year 2000.

Acting on the Congress' appropriation of $2 million for Parks in Peril, we've targeted some 40 projects this year which will help protect parks covering up to 12 million acres in Latin America.

Although A.I.D. funds have not yet begun to flow, this is the same issue that Mr. Sklar alluded to, with private monies we are getting some of these projects underway.

For each of the projects, we have detailed work plans, prepared jointly by ourselves and our partner organizations, which indicate the exact actions and costs of protection of each park.

This week in Guatemala, we have convened conservation land managers from Mexico and Central America to work out details of the specific park protection projects, and in three weeks in Venezuela, we have another work shop with NGO and government agencies from South America to look at the specific plans for implementing Parks in Peril.

We've been very effective in attracting the private sector match. You recall, it's a four to one public/private matching program. We set a goal of raising $500,000, and we expect to triple that goal in private match.

We did a mailing to the membership of The Nature Conservancy and got a 23 percent response, which is unheard of in direct mail, and I think this is a very direct, tangible and lasting way of——

Mr. **Obey**. Give me your mailing list.

Mr. **Barnard**. Right. We call it the cold fusion of direct mail. Parks in Peril satisfies, we feel, the demand of the American public to do something lasting and tangible for the rain forests.

The project has also received a positive response from A.I.D. as well. It's had outstanding acceptance from the Latin American community.

We have 23 non-governmental and governmental agencies helping us with designing the projects, identifying the sites, and developing the work plans, and hope to be implementing the work this year.

This whole approach is fundamentally different from one-time grants for park management because we build in the sustaining funding, and this is a critical point.

We're working hard to develop sustainable sources of local support for the parks so that these countries are not dependent on international assistance.

DEBT FOR NATURE SWAPS

To date, the most effective method for generating local funds for conservation is the debt for nature swap. There have been 12 debt for nature swaps since the first in Bolivia in 1987.

The Nature Conservancy and World Wildlife Fund have been involved in all but one of those swaps, and in the last two weeks alone, two swaps have been concluded, one in the Dominican Republic and one in Costa Rica.

The total of privately financed debt swaps now exceeds $50 million in face value. That's a large amount for conservation, although not a large amount for the debt problem.

These privately financed debt swaps are limited really by the availability of private donations to purchase the debt. Even if the debt is selling for 10 percent, to buy $10 million, you still need $1 million privately.

Debt gifts by commercial banks have been very slow in coming. There has been one gift so far of $250,000 of Costa Rican debt donated to us by Fleet Northstar Bank of Rhode Island.

I believe there are some others in the works. World Wildlife and TNC were both working on debt gifts, and we hope to have better news to report.

But if we hope to get debt swaps up to a scale where they really make a difference in the rate of deforestation, we need to think about some significantly bolder kinds of actions.

This committee took such action last week when it appropriated funds for a debt for nature swap in Panama. That swap is expected to convert $100 million of Panamanian commercial debt to protect the canal watershed and several million acres of tropical forests.

Without long term funding such as that, any short term conservation gains are simply going to vanish. To combat this, we're working to create what we call conservation trust funds on a country by country basis throughout Latin America.

These conservation trust funds would be analogous to our Land and Water Conservation Fund here in the United States but would receive capital through large scale debt for nature swaps.

Income from the trusts would secure funding for thousands of good jobs in the natural resource sector. The trust fund's Board of Trustees should include representatives of both the public and private sector, as will the Panamanian Trust Fund.

Having representation from the public and private sector is critical because it demonstrates that there's a new equation in international conservation.

There's something different from simply pouring money into programs which have failed in the past. There are two major mechanisms for establishing sustainable conservation trust funds: commercial debt buy-backs and bilateral debt conversion.

Publicly financed commercial debt buy-backs are just starting to be used. Last year, World Wildlife Fund received A.I.D. funds in Madagascar for a commercial buy-back, and your action last week in Panama is another long step in this direction.

But there are other techniques that need to be encouraged. We feel that the World Bank and Inter-American Development Bank should make preferential loans available to allow governments to repurchase their commercial debt expressly for the purpose of establishing a conservation trust fund in that country.

For example, in the Philippines, World Bank is about to make a $200 million loan to the Philippine government to repurchase $1.5 billion of the Philippines' commercial debt, with no environmental conditionality.

That debt will simply disappear. Clearly, it would not have been impossible in the planning stage to earmark $20 million of that loan to the Philippines to create a conservation trust fund for long term conservation efforts.

Additionally, bilateral debt could be used to create conservation trust funds by allowing a country's bilateral debt obligation to be converted into long term conservation bonds which would be deposited in a in-country trust account. While the Brady Plan suggests that banks and countries renegotiate their debts, the irony is that the U.S. Government offers little in the bargain..

The banks give up a portion of what is owed to them, the countries agree to pay the balance, yet the U.S. Government makes no significant contribution of its own.

We're not suggesting outright debt forgiveness of the U.S. bilateral debt. What we're suggesting is that a percentage of what's due be converted into new conservation bonds.

In other words, the repayment in dollars is waived, and repayment in local currency into a conservation trust fund is authorized.

The conversion would be conditional. As long as the payments are made on the new bonds, then the original debt would be considered to be satisfied.

If the payments were not made on the new conservation bonds, then the old debt would again be enforced. A.I.D. is owed $6.7 billion in Latin America alone. We suggest that $200 million, a small fraction of that total, could be converted into conservation trust funds this year at a minimal cost.

OMB, in its scoring of President Bush's action last year to forgive debt in sub-Saharan Africa, has shown that the budgetary impact of this is minimal. It scored only as the lost expected revenue to Treasury, and that's a critical point. Not what's due, but what is actually expected to be paid.

In the case of a $1 billion forgiveness in sub-Saharan Africa, the scoring was only $17 million. We estimate that $200 million of A.I.D. debt in Latin America could be converted into conservation trust funds this year with a $10 million to $20 million fiscal impact.

We ask the committee to support efforts to amend the Foreign Assistance Act, which would authorize the President to convert bilateral development assistance debt into conservation trust funds.

If we're successful in getting that authorization, this committee would be asked to appropriate funds for those bilateral conversions.

With this new authority, the Administration could convert debt in a mix of Latin American countries where deforestation is a critical problem, where arrearages on all of A.I.D. debt are interfering with current economic assistance, this whole issue of invoking Brooks-Alexander and the 260Q, and where debt relief is imperative for the overall economic recovery of the country.

A.I.D.'S BIODIVERSITY PERFORMANCE IN LATIN AMERICAN

The committee has also asked for our comments on A.I.D.'s performance in the area of biodiversity in Latin America. Responding to the directives from Congress, A.I.D. has made significant improvements in the last two years in its commitment to biodiversity protection.

We agree with World Wildlife Fund in saying that A.I.D. now realizes that biodiversity protection in the environment is here to stay.

One of the most important changes has been A.I.D.'s increased willingness to use the specialized knowledge of organizations such as ours in designing and implementing new projects.

There's an alphabet soup of projects out there which involve both international NGOs and national level NGOs, the park project in Jamaica, the RENARM project in Central America, FORESTA in Costa Rica, new projects such as SUBIR in Ecuador and MARENA in Guatemala.

A.I.D. has shown increased flexibility to collaborate in what we see as four vital program areas. The first, building local conservation organizations and training conservation leaders; the second, actually protecting and managing parks and reserves; the third, developing conservation information management systems through the support of conservation data centers, rapid ecological assessments, and biological inventories; and the fourth, long term funding through such mechanisms as debt for nature swaps.

Congress' directives to A.I.D. clearly had a positive effect, and we encourage you to continue the biodiversity earmark and to continue to encourage A.I.D. to integrate resource protection into its development assistance projects.

Simply to close, I'll say that biodiversity protection is an enormous challenge. It is linked to societal change and technological innovations.

Ultimately, people must recognize that conservation and sustainable use of natural resources are integral parts of society's business.

Economic justice and environmental justice are inseparable. Thank you for your leadership and your time today.

[The prepared statement of Mr. Barnard follows:]

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Latin America Program

STATEMENT OF GEOFFREY B. BARNARD
VICE PRESIDENT FOR THE NATURE CONSERVANCY
BEFORE THE HOUSE SUBCOMMITTEE ON FOREIGN OPERATIONS

April 3, 1990

Mr. Chairman, members of the Committee, on behalf of The Nature Conservancy, I want first to express our gratitude to you for choosing to focus your attention and considerable influence on the issue of biological diversity and its role in U.S. foreign policy.

My name is Geoff Barnard and I am Vice President for The Nature Conservancy's Latin American program. We are an international non-profit, land conservation organization, dedicated to the preservation of natural diversity through the protection of threatened species and ecosystems. In this country we own and manage over a million acres of private preserves. In partnership with public agencies both state and federal, we have helped protect over 3 million acres of critical wildlife habitat. We have taken our three stage process of identification, protection, and stewardship, and adapted it to fit the needs of developing conservation movements outside our borders.

On behalf of our 550,000 members, our Latin American partners, and our new President, John Sawhill, I thank you for this opportunity to present our views on these critical issues of biological diversity.

THE VALUE OF BIOLOGICAL DIVERSITY

The loss of biological diversity is the most prevalent and irreversible environmental problem facing this planet. Species extinction is rapidly accelerating. We have only begun to understand what the consequences of this lost wealth will mean.

Biodiversity is important to our foreign policy because it can determine the quality of life and economic sustainability in the developing world. It is not some esoteric terminology for scientists. In simplest terms, it is our global savings account, a pool of genetic wealth that someday we may need to draw upon. It is our ultimate safety net. Many of its great values are well known, yet more still remain a mystery.

A newly discovered wild maize brought back from Mexico by Wisconsin's own Professor Hugh Iltis resulted in an enormous breakthrough in corn evolution and has significant potential for the development of disease resistant domestic corn. The rosy periwinkle led scientists to a treatment of childhood leukemia. Digitalis, derived from the common foxglove plant, has saved the lives of enumerable heart patients. There are thousands of species yet to be discovered and studied, their benefits and utility to humankind unknown.

The international conservation challenge is well-documented and increasingly recognized as a crisis of world-wide significance. In Latin America, which contains approximately 60 percent of the world's remaining tropical forests, deforestation is now widely seen as a major threat to the social, economic and environmental stability of the hemisphere. The planetary consequences of the destruction of this resource, in terms of the greenhouse effect, ozone depletion, species loss and global warming, are critical to our fragile earth.

It is our view that the task internationally is to help provide the tools to the people and governments of sovereign nations so that they are equipped to protect their natural heritage within the context of a sustainable economic system.

PARKS IN PERIL

Last year, through the leadership of this subcommittee and with Congress's support, The Nature Conservancy launched Parks in Peril, a public/private partnership to safeguard the most important and imperiled natural areas in this hemisphere. By bringing conservation management to 20 critical parks and reserves each year, the Parks in Peril campaign will protect 200 key sites--more than 100 million acres--by the year 2000.

During the 1990s, Parks in Peril will achieve three critical goals:

- Build a basic conservation infrastructure in the hemisphere's 200 most imperiled tropical ecosystems;
- Integrate these protected areas into the economic and cultural lives of their societies;
- Create long-term funding mechanisms to sustain the local management of these areas.

A comprehensive strategy for the protection of our natural lands must be embraced by everyone. The Parks in Peril campaign provides such a strategy. It is achievable. It is based on political and economic realities. It brings all conservation actors--public and private, north and south--together on a common agenda. And it is the very least that must be accomplished in the next ten years to protect that part of the Americas that still awaits discovery.

Acting on the Congress' appropriation last year of $2.0 million for Parks in Peril, we have begun projects which will help protect parks covering up to 12 million acres in 15 Latin American countries by the end of this year. For example, in Bolivia, this year's work plan will launch the first real park protection of Amboro and Noel Kempff National Parks, which comprise roughly 2.5 million acres of threatened tropical forest and Andean habitats. For each of the projects, we have detailed work plans prepared jointly by ourselves and our partner organizations, which indicate the exact actions and costs of protection of each park.

Because of the matching challenge presented us by Congress we have been enormously effective in attracting private sector donations for Parks in Peril. We established the target goal of $500,000 in private donations, and in fact we expect to triple that goal. In a mailing to the membership of The Nature Conservancy we achieved a 23% response, unheard of for direct mail. We are also launching an Adopt-an-Acre program to satisfy the demand of thousands of Americans who want to do something tangible and lasting for the rainforest. The demand from school groups is amazing, especially in these weeks prior to Earth Day.

The Parks in Peril project has received a positive response from AID, as well. The Parks in Peril concept -- direct action to save the rainforest -- has an enormous appeal and has struck an important chord in the American public.

It also has outstanding acceptance from the Latin America community. We have had cooperation from 23 non-governmental and governmental organizations throughout Latin America in identifying the sites, developing the work plans, and implementing the Parks in Peril project.

The Parks in Peril approach is fundamentally different from one-time grants for park protection because it develops continuous funding mechanisms to support conservation over the long term. Each protected area enters a cycle in which the initial emergency international assistance is replaced with sustaining sources of local support.

We are working hard to find those sustaining sources of local support. To date, the most effective method for generating local funds for conservation is the debt-for-nature swap.

DEBT-FOR-NATURE SWAPS

Driven by exploding populations, poverty, and the need to generate foreign exchange to pay the debt, Latin American countries are accelerating exploitation of the remaining natural lands in non-sustainable ways, leading to degraded soils, polluted waters, and contributing to global warming, ozone depletion and the production of greenhouse gases.

Latin America currently faces two major crises of unprecedented magnitude: the destruction of their natural resources and the overwhelming burden of international debt.

Proposed in 1984 by Thomas Lovejoy, the first debt-for-nature swap was undertaken in Bolivia in 1987. Subsequently, there have been eleven additional private swaps. In these cases, private funds have been raised to purchase the country's commercial debt on the secondary market at prices ranging from 11 percent to 33 percent of face value.

The debt is then converted for conservation projects, in country, to fund a wide range of needs: national park land acquisition, management of existing and newly created parks, research and environmental education, operations of private conservation organizations, and pilot projects and studies in sustainable use of natural resources.

Recently we have concluded debt swaps in Ecuador, the Dominican Republic and Costa Rica. There is a new debt swap quota established in Argentina, and conversations are underway in a host of other countries, including Mexico, Jamaica, and Peru.

While enormously useful in making financial resources available for conservation, private debt-for-nature swaps are limited by the availability of private donations to purchase the discounted debt.

Now is the time to think about bolder actions if we hope to have a significant impact on the rate of tropical habitat loss.

THE LATIN AMERICAN CONSERVATION TRUST FUNDS

This Committee took an important step last week when it appropriated funds for a debt-for-nature swap in Panama. That swap is expected to convert $100 million in Panamanian commercial debt to protect the Canal watershed and several million acres of tropical forests.

Without long-term funding like this, few conservation gains will be permanent. They will vanish like the wake of a ship.

To combat this--to put conservation on a sustaining economic footing--we are working to create Conservation Trust Funds, throughout Latin America, on a country-by-country basis. These Conservation Trust Funds would be similar to our own Land and Water Conservation Fund, one of the most successful pieces of conservation legislation ever enacted.

The Conservation Trust Funds we propose would receive capital through large scale debt-for-nature swaps. Income from the trusts would guarantee secure funding for thousands of good jobs in the natural resource sector. The Trust Funds' boards of trustees should include representatives of both the public and private sectors, just as the proposed Panama Conservation Trust Fund does.

This new partnership between private conservation organizations in developing countries and their government counterparts is a crucial element. If you and we are to be satisfied that money from Conservation Trust Funds will actually save the rainforests, we must be convinced that it will not merely disappear into bureaucratic coffers. There must be a new equation. That new equation includes, and depends on, the private sector NGOs.

The time to create Conservation Trust Funds is now.

It is clear that some type of massive debt readjustment will be required for Latin American economies to become viable and to provide for sustainable economic growth and political stability in the region. The key point is this: Restructuring agreements will inevitably involve concessions by both creditors and debtors. At the time these concessions are negotiated, there will be an extraordinary, one-time opportunity to direct a small fraction of the total debt into a Conservation Trust Fund in that country.

There are two major mechanisms for establishing Conservation Trust Funds: commercial debt buy backs and bilateral debt conversion.

Commercial debt buy-backs are just starting to be used. In Madagascar, WWF received USAID funds to purchase commercial debt for projects there. Your action last week on the debt-for-nature swap provision within the Panama supplemental aid package took another long step towards creating sustainable funding sources for conservation in developing countries.

However, other techniques must be encouraged as well. The World Bank and the Interamerican Development Bank should make loans available to allow governments to repurchase commercial debt expressly for the purpose of converting that debt into Conservation Trust Funds. The World Bank is about to make a $200 million loan to the Philippines **as part of a package to** repurchase $1.5 billion of commercial bank debt, with no environmental conditions. Clearly, $20 million of this loan could have been earmarked **to purchase debt specifically** for the creation of a Conservation Trust Fund.

Recommendation

We urge the Committee to encourage World Bank and the InterAmerican Development Bank, to make loans to Latin American countries for the purpose of repurchasing commercial debt to convert to Conservation Trust Funds.

BILATERAL DEBT CONVERSION

Bilateral debt is an additional option that should be used to create Conservation Trust Funds. While the Brady Plan has encouraged commercial banks to recognize the true value of their Third World debt, and encouraged countries to negotiate reduced payments with their creditors, the obvious, and ironic fact is that the U.S. Government offers little in the bargain. The banks give up a portion of what is owed them, the countries agree to pay the balance, yet the U.S. Government fails to make any significant contributions of its own.

We are not suggesting outright debt forgiveness. We are suggesting that a percentage of the debt due be converted into new "Conservation Bonds" to be held by the Conservation Trust Fund in each country. The conversion would be conditional: as long as the payments are made on the Conservation Bonds, then the original debt would be considered to be satisfied. If payments were not made on the new bonds, then the old debt would again be enforced.

Why would this appeal to a country? First, the payments on the Conservation Bonds will be significantly less than what was due on the original debt, due to a renegotiated lower interest rate and longer maturity. There is a true cash savings to the country. Secondly, scarce foreign exchange earned from exports is not paid overseas. Thirdly, the money is kept in-country to create jobs in the natural resource sector in parks management, forestry, reforestation, watershed management, and tourism. Fourth, by spreading the payments out over many years, the Conservation Trust Fund is non-inflationary to the local economy. Fifth, by converting external debt to an internal obligation, the country's overall credit rating improves. Finally, the country is making a wise choice to invest in management and sustained use of its natural resources.

USAID is owed $6.7 billion dollars in Latin America alone. We suggest that $200 million of that bilateral debt could be converted into Conservation Trust Funds this year at minimal cost.

OMB, in its scoring of President Bush's action last year to forgive debt owed by sub-Saharan Africa, has shown that the budgetary impact of such an action is minimal: it is scored only as the lost expected revenue to Treasury. In the case of the $1 billion sub-Saharan Africa debt, the scoring was only $17 million.

We estimate that $200 million of USAID debt in Latin America and the Caribbean could be converted into Conservation Trust Funds this year with only a $10-20 million fiscal impact.

Recommendation

> **We urge the Committee to support efforts to amend the Foreign Assistance Act by authorizing the President to convert bilateral development assistance debt into Conservation Trust Funds. If we are successful in getting that authorization, this committee would be asked to appropriate funds for such bilateral conversions.**

With this authority, the Administration could convert debt in a mix of countries where deforestation is critical, where arrearages on old USAID debt are interfering with current economic assistance (Brooks-Alexander amendment, etc.), and where debt relief is imperative for overall economic recovery.

Even Brazil, which currently would not qualify for development assistance from the U.S., has $1 billion in old debt from the sixties.

What foreign policy value is there in belaboring the Latin American economies -- and their environments -- with these debts? Why not turn some of it into Conservation Trust Funds?

OVERSIGHT OF UNITED STATES AGENCY FOR INTERNATIONAL DEVELOPMENT

Responding to directives from Congress, the U.S. Agency for International Development has made significant improvements over the last 2-3 years in their commitment to biodiversity protection.

Congress set the stage for this by enacting Sections 118 and 119 of the Foreign Assistance Act of 1961. More recently, the biodiversity earmark approved by this committee has provided the stimulus for far more concrete actions by AID.

One of the most important changes in AID programming over the last two years has been their increased willingness to use the specialized knowledge and experience of private sector conservation organizations such as World Wildlife Fund and The Nature Conservancy.

The Nature Conservancy is working closely with AID missions on biodiversity initiatives that we and our partner NGOs are implementing.

What is perhaps most important about these projects is that they are not "creatures of AID," not fully dependent on AID, therefore not likely to disappear when AID support ends. Rather, these new generation projects involve international NGOs, local NGOs and counterpart agencies in partnership, building in continuity of action and success.

A case in point is the Protected Areas Resources Conservation (PARC) project in Jamaica. This projects launches a Jamaican National Parks system and actual management on the first two parks, builds a local NGO--the Jamaican Conservation and Development Trust--as a key counterpart to the government resource agency, establishes a Jamaican Conservation Trust Fund using the debt swap mechanism, and funds the initial stage of a Conservation Data Center to prioritize areas and species for protection. Built into the structure of the project are the elements and actors needed for continuity.

We support the recent announcement by Acting Administrator Edelmann that AID has taken the lead in supporting the protection of the Mbaracayú, a 150,000 tract of tropical forest in eastern Paraguay.

We are also a partner, with World Wildlife Fund and World Resources Institute, in the implementation of the AID centrally funded Biodiversity Support Project. This project supplies technical assistance and training throughout the world. The Conservancy is benefitting from this partnership as we begin to expand our international work to the Pacific islands and beyond.

AID has shown an increased flexibility to collaborate with us in four vital program areas:

1) building local conservation PVOs (NGOs) and training conservation leaders in Lain American countries;

2) protecting and managing parks and reserves, both through mission funded projects such as PARC, RENARM, and FORESTA, and through centrally funded projects such as Parks in

Peril;

3) developing conservation information management systems, through the support of Conservation Data Centers, rapid ecological assessments, and biological field inventories;

4) long-term funding to support biodiversity -- protection through innovative mechanisms such as the FORESTA local currency endowment fund for Braulio Carillo National Park, and a debt-for-nature swap for La Amistad National Park management endowment both in Costa Rica.

We want to encourage AID to continue to increase its assistance to on-the-ground actions of this type, and we commit ourselves to cooperative partnerships with AID which achieve our mutual goals.

Congress' mandate to AID has clearly had a positive effect. Now, in the face of ever-widening environmental crises in the tropical forests of the world, all of us - Congress, AID and the conservation community - must redouble our efforts.

Recommendation:

We urge the committee to strengthen its mandate to AID by increasing biodiversity funding and continuing to encourage AID to integrate resource protection into its development assistance projects.

Preserving the biological diversity of the planet is an enormous challenge. It will require strong leadership, technological innovations, societal changes, and conservation actions. People must recognize that conservation and wise use of natural resources are vital, integral parts of society's business.
Economic justice and environmental justice are inseparable.

Thank-you for your leadership and for your time today.

Mr. OBEY. Thank you. Let me simply say that I have about five questions I wanted to ask you, but because of the time I am simply going to forego the questioning here.

I will give you the questions for the record that I had in mind, and you can respond for the record. I very much appreciate all of you coming today.

[The information follows:]

Questions for the Record From Mr. Obey

Submitted to Glenn Prickett, NRDC and Scott Sklar, US/ECRE

TROPICAL FORESTRY ACTION PLAN

QUESTION. Outline your concerns regarding the Tropical Forestry Action Plan (TFAP).

Mr. PRICKETT'S response. Despite the laudable intentions of TFAP, NRDC has grave doubts about the quality of the country plans that are beginning to emerge from the TFAP process. Across the board, TFAP has become a narrowly-defined investment planning exercise for the forestry sector. To date, country plans have paid little attention to critical cross-sectoral policy and institutional issues driving deforestation in most tropical countries. Most plans do not adequately address the need for policy reform in such areas as land tenure, land-use planning, population, and energy, among others.

TFAP's narrow focus on investment planning has resulted largely from a closed process driven by forestry professionals that has systematically slighted the input of other government agencies, nongovernmental organizations (NGOs), and local communities. In very few cases have country review teams solicited the advice and input of local communities and NGOs in designing projects for TFAP funding. Moreover, in almost all cases documentation on the TFAP process has been unavailable to interested NGOs and members of the public. Review teams have been composed largely of professional foresters, and, consequently, have not focused adequately on investment, policy and institutional issues outside of the forestry sector.

NRDC has joined with NGOs around the world in calling for a moratorium on donor support for TFAP projects, until significant reforms have been made in the TFAP process. We have called on the U.S. Executive Director of the World Bank to offer to chair a review of the Bank's involvement in TFAP and suggest reforms. We recommend reform in following areas:

Scope.—The scope of TFAP must be broadened to identify needed policy and institutional reforms at the country level. Country plans should establish concrete timetables for such reforms.

Public Participation.—The TFAP process must be opened to participation by NGOs and local communities. Review teams and governments should solicit the participation of these groups in all stages of the TFAP planning process. Governments should be required to make all TFAP documentation available to the public and to hold public hearings on country plans during their preparation and upon their completion.

Oversight.—At a global level, in order to encourage TFAP review teams to focus on wider range of issues, the TFAP secretariat should be removed from FAO and relocated at UNEP. The existing TFAP staff at FAO should continue to play a supporting role in coordinating country planning exercises. At a national level, TFAP guidelines should require governments to establish review committees, consisting of a wide range of government agencies, indigenous peoples organizations, academics, NGOs, and the private sector, to oversee all stages of the TFAP process.

Mr. SKLAR's response. Concerns regarding the Tropical Forestry Action Plan (TFAP) involve disregard to private sector options to provide incentives to maintain forests. Installation of biomass facilities based upon sustainable yield forests may institutionalize a system to ensure that forests are maintained and expanded. Obviously, a side benefit would be extra electric or thermal energy generated to countries with extreme energy shortages and high energy imports.

IDA AND WORLD BANK ENVIRONMENTAL EFFORTS

QUESTION. Outline your assessment of the recent IDA replenishment, and its sensitivity to environmental concerns.

Outline your assessment of the World Bank's proposed new global environmental fund.

Mr. PRICKETT's response. Overall, the IDA deputies, and particularly the U.S. Treasury Department, are to be commended for establishing a comprehensive environmental mandate for IDA in the coming years. Largely due to the insistence of the U.S., the IDA-9 report contains detailed language on environment in a number of areas.

Among other things, the report requires that the Bank make all environmental assessments (EAs) available to Executive Directors and the public at least 180 days before loan presentation to the Board. Also, the report calls on the Bank to increase its professional staff expertise in energy efficiency and renewable energy, to expand energy planning assistance to include end-use efficiency and renewable energy, and to further integrate the activities of the Energy Sector Management Assistance Program (ESMAP) into the Bank's lending operations.

Our one concern about the IDA-9 report is its support for the TFAP process and its direction that the Bank increase IDA forestry lending under TFAP. As discussed in my response to your first question, we are calling for a moratorium on all Bank support for TFAP until a comprehensive review, chaired by the U.S. Executive Director, has identified needed reforms in the TFAP process. We urge the Subcommittee to call on the U.S. Executive Director to offer to chair such a review.

As I described in my written statement, NRDC supports the principle of additional funding for global environmental issues and feels that the Bank can play an important role. However, we have two serious concerns about the Bank's current proposal for a new environmental facility.

First, it is unclear from the Bank's proposal how operations funded under the new facility would relate to IDA and IBRD operations in critical sectors such as forestry and energy. The Bank must reexamine its existing portfolios to ensure that existing operations are not in conflict with the goals of global environmental protection. For example, the Bank has committed to more than triple its lending in the forestry sector over the next several years. However, there is no indication that the Bank has moderated its traditional focus on industrial timber extraction. A new facility would be justified only if it leverages significant reforms in the Bank's operations under IDA and IBRD, such as greater support for end-use energy efficiency programs and decreased emphasis on industrial timber extraction.

Second, the proposal does not address the urgent need to encourage greater public participation in the Bank's operations. Failure to encourage the participation of local communities and NGOs in the identification, preparation and implementation of projects has led to environmentally and socially disastrous operations in the past. The Bank still systematically withholds basic documents on its operations from the public in borrowing and donor countries. A new facility, operating under these same flawed principles, promises to be counterproductive.

Mr. SKLAR's response. Concerns regarding IDA replenishment and its sensitivity to environment and the World Bank's proposed new global environmental fund involve the fact that the programs are absolutely made without input from renewable energy, energy efficiency, or environmental review in a formal outreach process. While IDA and the World Bank are trying to respond to Congressional interest in the environment, the enclosed study recently prepared by US/ECRE shows a poor record. I believe the environmental fund, if tweaked to become a loan-guarantee revolving fund, would be the most practical approach. But the World Bank has yet to enter this more pragmatic arena to encourage environmentally-sensitive renewable energy and energy efficiency projects.

A.I.D. OFFICE OF ENERGY

QUESTION. How has A.I.D. responded to the Committee's direction to increase funding for the Office of Energy and its activities, and to increase the ability to provide technical advice to key developing countries?

Mr. PRICKETT's response. As I describe in my written statement, AID has not followed the Committee's direction to fund the Office of Energy at a level of $20 million in FY 1990. AID's FY 1991 CP sets the Office's FY 1990 budget at roughly $15 million in FY 1990 and proposes a subsequent decrease in FY 1991 to roughly $13 million.

A strong, well-staffed Office of Energy will be critical in providing support to AID's missions and working directly with countries in developing and implementing state-of-the-art energy planning, energy efficiency and renewable energy programs. The Committee, in its oversight role, should insist that AID meet the Congressional target of $20 million for FY 1990. Furthermore, the Committee should direct AID in its appropriations for FY 1991 to further increase the Office's budget to $30 million.

Mr. SKLAR's response. AID has responded half-heartedly to the Subcommittee's directed increase. The Science & Technology Office of Energy has only received $5 million of the $10 million directed. At present a number of projects have been discussed to enhance training, information and pre-feasibility support. They have yet to be consummated. The Subcommittee should direct the AID Science & Technology Division Office of Energy to receive $20 million in FY 1991, and the activities should include the establishment of a pre-feasibility and training fund for renewable energy and energy efficiency applications in partnership with the U.S. private sector in these aresa and the U.S./AID recipient countries.

A.I.D. CONTRACTOR ABUSES

QUESTION. The Committee has been made aware of potential conflict of interest situations where A.I.D. contractors are manipulating the system to their financial advantage, particularly in Asia. What do you know of these situations?

Mr. PRICKETT's response. I have no detailed knowledge of any conflict of interest situations among AID contractors.

Mr. SKLAR's response. AID has contracted with consulting firms that are profit-making entities that have business interests in the regions of which they serve. They have bid against U.S. companies for certain projects and the Subcommittee should direct AID to develop formal agreements limiting their profit-making activities if they are a multiyear support contractor to any program. Support contractors are not individuals but larger consulting firms with multiyear contracts over a wide range of responsibilities.

TUESDAY, APRIL 3, 1990.

ADMINISTRATION WITNESSES

MARK EDELMAN, DEPUTY ADMINISTRATOR, AGENCY FOR INTERNATIONAL DEVELOPMENT

RICHARD SMITH, DEPUTY ASSISTANT SECRETARY, BUREAU FOR OCEANS, AND INTERNATIONAL ENVIRONMENTAL AND SCIENTIFIC AFFAIRS, DEPARTMENT OF STATE

FRANK VUKMANIC, DIRECTOR, OFFICE OF MILTILATERĀL DEVELOPMENT BANKS, DEPARTMENT OF THE TREASURY

CHAIRMAN'S OPENING STATEMENT

Mr. OBEY. If I could now ask the Administration witnesses to come forward, Mr. Richard Smith, Deputy Assistant Secretary, Bureau for Oceans and International Environment and Scientific Affairs, from the Department of State; from the Department of Treasury, Mr. Frank Vukmanic, Director, Office of Multilateral Development Banks; and from the Agency for International Development, Mr. Mark Edelman, Deputy Administrator, Agency for International Development.

Mr. Edelman, we have all of your statements. They will be inserted in the record. If you could each take about five minutes to summarize your statements. We will try to get right to the questions, and maybe I can still get to the meeting I'm supposed to be at with Mr. Baker, but I doubt it. Go ahead.

MR. EDELMAN'S OPENING STATEMENT

Mr. EDELMAN. Thank you, Mr. Chairman. Let me not keep you from the Secretary of State. At least, don't let him know I'm the one who did.

Mr. OBEY. I'll tell him it's your fault.

Mr. EDELMAN. I appreciate this opportunity to testify before this committee today, Mr. Chairman, because the issue of A.I.D.'s efforts to help developing countries manage their environment and natural resources is one in which I have a very strong commitment and interest.

It's no secret that A.I.D. places a premium on helping developing nations achieve economic growth. In fact, without economic growth, there can ultimately be no sustainable development gains.

Over the years, there has been a perception that economic development automatically came at the expense of the environment.

Regrettably, that's because that was, in some instances, the case. But it need not be, as we all now know. I'm proud to be able to say that, especially among development agencies, A.I.D. has been way ahead of the pack in understanding and reacting to global environmental concerns.

Today, A.I.D. is among the leaders of development agencies in making sure that the environment is front and center on our development agenda.

In fact, all of our development projects are subjected to an environmental impact review before they are implemented in the field.

However, A.I.D. has gone beyond just making sure that our development projects don't harm the environment. A.I.D. has taken the lead in supporting projects which actually enhance environmental sustainability, such as debt for nature swaps, and alternative agriculture solutions to slash and burn techniques which scar the earth, deplete the rain forests, and contribute to the potential for climate change and loss of biological diversity.

Beyond that, we've recognized that as committed as we are to economic growth, ultimately there can be no economic sustainability without environmental sustainability.

The truth of that statement is borne out in the developing nations that have plundered their natural resources for short term gain and in the environmental degradation found in eastern Europe.

ECONOMIC AND ENVIRONMENTAL POLICIES FOR SUSTAINABILITY

While the environmental degradation of eastern Europe is the result of complex factors developed over an extended period of time, one underlying cause is clear: misguided economic and regulatory policies.

I believe that the use of market forces must be an increasingly important and integral component of A.I.D.'s environment program.

Although a free and open market is certainly no cure for the environment, as western development has demonstrated, economic incentives and rational economic policies which promote conservation are critical to achieving significant change in developing nations.

Unless we are able to persuade governments to change these policies, policies which encourage the squandering of natural resources and actually subsidize short term exploitation for short term gain, there can be no base for any significant sustainable development.

Likewise, the issues of reforestation, environmental sustainability and biodiversity, which play such a critical role in any successful development strategy, face many of the same challenges that we do in our work to encourage sustainable development, the challenge of giving people choices.

If given a choice between slash and burn techniques which ultimately destroy the soil and agricultural techniques that will bring more produce for a longer time without damaging the land, a farmer will choose the latter.

Without that choice, a farmer will slash and burn until there is nothing left to slash or burn.

People don't cut trees just for fun. They cut trees because it brings cash or clears the land for pasture or helps to establish title to the land.

If given a feasible alternative, people and governments wouldn't need to exploit these rain forests or hunt rare and exotic animals.

If that is the only way to bring needed cash to buy food or medicine for sick and hungry babies, then the choice for these people is not whether or not to shoot the last remaining rhino but when and where to do it.

So the question becomes how do we change the need to exploit precious natural resources? The answer is policies. We need to help developing nations make the politically tough choice to change policies that foster environmental degradation into policies that help sustain precious natural resources.

Because a nation is only as rich as its resources, and as these resources are depleted, so is a nation's chances of ever bringing economic prosperity to its people.

Failing to provide viable economic options, the attitude will continue to be one of environmental sustainability be damned, I've got a family to feed.

Quite frankly, who could blame them for choosing short-term survival over long-term environmental improvement? Finally, and perhaps most importantly, is the need for all of us here in Washington and in the field to develop what I call an environmental attitude.

Environmental concerns must be integrated into all we do. We cannot be satisfied with spending a certain percentage or sum of our budget on environmental projects.

Rather, we must improve the training and understanding of all of A.I.D.'s employees so that environmental concerns become a routine part of project design and policy dialogue.

After years of effort, we have reached this level with our economic dialogue, and we need to do the same thing with the environment.

Developing the same knee jerk response about environmental policies is worth more than I could put a price tag on and will take us a long way toward reaching our goal of environmental sustainability and biodiversity around the world.

Now, does that mean that A.I.D. is doing everything right by the environment? Certainly not. There's much more that we can and want to do, which leads to the challenge of trying to figure out how to target our resources on issues and countries which will most dramatically increase the effectiveness of A.I.D.'s environment program.

But I am buoyed by my conviction that A.I.D. is actively pursuing avenues to achieve an effective blend of economic growth and environmental sustainability in the developing nations where we work, and I look forward to continuing to work with Congress toward that end.

[The prepared statement of Mr. Edelman follows:]

STATEMENT OF

THE HONORABLE
MARK L. EDELMAN
DEPUTY ADMINISTRATOR
AGENCY FOR INTERNATIONAL DEVELOPMENT

BEFORE THE

COMMITTEE ON APPROPRIATIONS
SUBCOMMITTEE ON FOREIGN OPERATIONS
UNITED STATES HOUSE OF REPRESENTATIVES

APRIL 3, 1990

Thank you Mr. Chairman. I appreciate the opportunity to testify before this subcommittee on A.I.D.'s efforts to help developing countries manage their environment and natural resources. Concern for the environment in developing and developed countries has grown dramatically in recent years as the global impact of local environmental degradation has become more evident. Depletion of stratospheric ozone, the potential for climate change, loss of biological diversity, and destruction of tropical rain forests all dramatically illustrate the complexity and urgency of protecting the environment.

Although the long-term effects of environmental degradation are often global, the causes are local, as are the most immediate effects. Rapid population growth, extreme poverty, inequitable access to land and other resources, rapid urbanization, and inadequate policies ultimately result in air and water pollution, soil erosion, loss of biodiversity, and destruction of tropical forests, threatening to alter irreversibly the functioning of normal ecosystems.

While acknowledging the limits of any single development assistance agency in the face of such complex and pervasive problems, A.I.D. is strongly committed to addressing these difficult issues and will continue to help developing countries conserve and protect their environment and natural resources. By helping them, we are also protecting future generations of Americans. A.I.D. has long recognized the link between environmental protection, the management of natural resources and economic development. We have been joined by a growing number of individuals and institutions which accept that environmental protection is an integral and critical component of economic growth. Protection of the environment and environmentally sound management of exploited natural resources is fully consistent with A.I.D.'s mandate to promote broad-based economic growth.

Our environmental leadership is based on our ability to fully and consistently incorporate environmental considerations into every development assistance activity we support. We will continue to emphasize the importance of the environment in everything we do. I place high priority on increasing our in-house capacity to address the environmental issues, including hiring additional experts in these fields and expanding our training program for A.I.D.'s technical and senior staff. In regard to our new authority to use program funds to increase the number of A.I.D. personnel with environmental expertise, an Agency-wide task force has been formed to prepare guidance on the implementation of this authority. At the same time, another unit within A.I.D. is studying the relationship between program and workforce and ways in which the Agency can better respond to critical workforce requirements.

Policy dialogue and public awareness are absolutely critical to A.I.D.'s efforts to protect the environment. Project assistance, although important, will never be sufficient to address the tremendous environmental problems that developing nations face. When A.I.D. convinces a Minister of Finance that conserving natural resources is critical to economic growth, and successfully encourages a Minister of Environment to incorporate economics into conservation activities, we have gone a long way toward promoting environmentally sound economic growth, and have accomplished more than could be done through a single conventional project.

The use of market forces must be an increasingly important and integral component of A.I.D.'s environment program. Although a free and open market is certainly no cure for environmental problems, as Western development has demonstrated, economic incentives and rational economic policies which promote conservation are critical to achieving significant environmenal change in developing countries.

A mother who must choose between saving the last remaining tree and gathering fuelwood to cook for her child will always choose to feed her child. With no alternative source of fuel, her child's short-term survival will take precedence over any longer-term concerns for environmental degradation. Her child comes first, period. No one wants to destroy the environment, but natural resources will be used sustainably only if people have an alternative means of meeting their most basic needs.

Market forces and economic instruments are critical to ensuring that those who bear the cost of conservation also receive the resulting stream of benefits. Inhabitants living in and around forests, wetlands, and coastal zones, who exercise the real power over the use of natural resources, should be provided incentives to manage these resources sustainably for their own benefit.

Removing incentives which promote the destruction of natural resources is equally important. Inappropriate land tenure and tax policies, for example, provide incentives which are known to contribute significantly to deforestation in the tropics.

Let me now turn to some specific A.I.D. environment programs. A.I.D. continues to provide strong leadership in support of tropical forestry, forest management and reforestation, environmental planning and education, and improved industrial and urban pollution control. We are expanding our efforts to address urban environmental problems and are updating and expanding our pest management guidelines to help promote environmentally sound agriculture. We continue to expand our efforts to address global issues such as the potential for climate change and the loss of biological diversity.

A.I.D.'s efforts to address the problem of potential climate change are reflected in support for forest management, reforestation, renewable energy, and energy conservation. A.I.D. plans to obligate $248 million for these activities in FY 1991 and $225 million in FY 1990, up from $185 million in FY 1989.

Some specific examples of our climate change activities will illustrate the range of our efforts in this area. A.I.D. is currently designing a program which will assist Brazil in promoting sustainable forest management and sustainable resource use policies and energy efficiency improvements. We will also provide an in-country forest policy/climate change adviser for the A.I.D. mission in Brasilia. Funding for this program in FY 1990 is expected to be on the order of $1 million. In Indonesia, A.I.D. is developing a new $18.5 million Environment and Natural Resources project. The principal focus is on forestry policy, including the reform of the forest concession system and field oriented activities designed to demonstrate sustainable forest management. In Poland, A.I.D. is working with the U.S. Department of Energy on the retrofit of a coal power plant to reduce sulphur and nitrogen oxide emissions, and with EPA on an air monitoring system for Krakow. We are funding a Global Energy Efficiency Initiative to develop project concepts on energy efficiency in key countries. This will include assistance in the design of projects to promote improved power sector investments (least-cost energy planning), increased end-use efficiency, and the promotion of policy reforms, especially in the areas of energy pricing and private power investment. We are also supporting an energy efficiency initiative with similar objectives targeted to Central America.

Energy efficiency and energy conservation are important elements in our climate change program. A.I.D. expects to obligate $144 million in FY 1990 and $153 million in FY 1991 for renewable energy and energy efficiency and conservation. We are promoting the use of new, higher efficiency technologies and management strategies, including reliance on rational pricing and greater involvement of the private sector in all facets of energy production, distribution, and use. We have provided energy conservation services to more than 25 countries, emphasizing conservation primarily in the industrial and electricity sectors, but also undertaking programs in the building and transportation sectors. For example, we are funding a $3 million "Energy Conservation Management" Project which focuses on energy conservation in buildings. In India, we are supporting research and rapid commercialization of more efficient and renewable energy systems and are joining with the World Bank in an assessment of the power sector.

Renewable energy sources offer an important alternative to fossil fuel use, which are a major source of greenhouse gas emissions. A.I.D. is supporting a variety of renewable energy projects in Egypt, India, Pakistan, and Morocco, each emphasizing in varying degrees wind, solar, photovoltaics, biomass, household fuels, and technology assessment. Our program focuses on developing sustainable, commercial projects encouraging increased involvement of the private sector and creation of appropriate policies.

I would like next to describe our biological diversity conservation efforts which are a growing component of our natural resource management portfolio. The challenge to A.I.D. is to help developing countries protect and promote the sustainable use of threatened biological resources that provide the raw materials for their economic growth. In response to the accelerating threats to these resources, A.I.D. has expanded efforts to protect and maintain wildlife habitats. We are supporting the establishment of the Zubiya Wildlife Reserve in Jordan, the Hol Chan Marine Reserve in Belize, and the Maya Biosphere Reserve in Guatemala. We are working with the Missouri Botanical Garden to establish a national park on Madagascar's Masoala Peninsula, and are helping to develop management plans for five protected areas in Burundi. A.I.D. will join with the World Bank and the Nature Conservancy to establish the Mbaracayu Nature Reserve in eastern Paraguay.

Having confirmed A.I.D.'s support for parks and protected areas, let me emphasize that I believe that the most important efforts to conserve biological diversity will take place outside the boundaries of these areas. Parks clearly represent the critical core of biodiversity conservation efforts, but they are insufficient in themselves to conserve most biological resources. Efforts to promote the sustainable use of resources will, in the long-term, have a greater impact on conserving biodiversity than creating parks which exclude people from resources they believe are rightfully theirs. Changes in misguided tax policies and removing structural flaws in royalty and license fees would have a tremendous beneficial impact on biodiversity. For example, through inappropriate tax policies the Indonesian government has sacrificed nearly $3 billion in timber revenues in four years because the price of forest concessions do not reflect the true value of harvested timber. Through policy reform, the Indonesian government could promote more rationale use of resources, support forest conservation, and generate billions of dollars in additional revenues. Similar circumstances can be found in Brazil, Malaysia, Thailand, and the Philippines.

Therefore, in addition to our activities focusing on habitat and species protection, A.I.D. supports efforts to strengthen legislation, policies, and institutions relevant to biodiversity conservation as well as environmental education and agroforestry for sustainable agriculture in buffer zones surrounding parks. Total obligations for biodiversity, expected to be $42.9 million in FY 1990, will continue to grow and become an increasingly integral component of our broader environmental efforts.

Before closing, I would like to mention A.I.D.'s environment program in the context of a changing world. The recent events in Eastern Europe bear two messages relevant to the topic of today's testimony. First, these changes have highlighted distant environmental problems that could affect our own lives. Second is the important role of open markets in a pluralistic society in protecting the environment.

The events in Eastern Europe can not be divorced from the tremendous environmental problems in those countries. High levels of pollution, and the inability of the central governments to improve the environment, surely were contributing factors to the mass dissatisfaction with the leadership which eventually resulted in the popular uprisings.

While the environmental degradation in Eastern Europe is the result of complex factors developing over an extended period of time, one underlying cause is clear: misguided economic and regulatory policies. With centralized economies, the Eastern European nations could not harness the power of market forces or provide the social incentives necessary to reverse the extensive environmental damage caused over a 40 year period of misrule. The sad state of the environment in these centralized economies graphically illustrates the potential power of market forces to conserve natural resources and protect the environment.

Given the magnitude of the environmental problems faced by developing countries, A.I.D. must recognize its limitations and design realistic approaches to resource conservation consistent with our mandate. Even as we expands our environmental program, we should continue to leverage resources through collaboration with other donors and work to ensure their support for environmentally sound development. For example, A.I.D. was instrumental in forming the environment working group in the Development Assistance Committee of the Organization for Economic Cooperation and Development to expand cooperation between bilateral donors. Coordination through this group has resulted in greater harmonization of environmental procedures between the bilateral donors. A.I.D. continues its efforts to improve the environmental performance of the multilateral development banks.

Finally, underlying all these activities, A.I.D. continues to be the leader in the donor community in ensuring that all of our development assistance activities are environmentally sound. Through A.I.D.'s formal environmental procedures, first adopted in 1976, all of our projects undergo an Initial Environmental Examination (IEE) during the project identification phase. If the IEE indicates that significant environmental effects are likely, an Environmental Assessment (EA) is conducted to identify mitigating measures or environmental safeguards that are to be incorporated into the project design. A.I.D., as the first bilateral aid agency to adopt formal environmental procedures, continues to set the standard for all the major bilateral donors.

Mr. **Obey**. Thank you very much.

Mr. Smith?

Mr. Smith's Opening Statement

Mr. **Smith**. Thank you, Mr. Chairman.

I welcome the opportunity today to talk about international environmental issues. In his recent presentation on our international environmental policy to the National Governors Association, Secretary Baker said, "environmental threats respect no border."

As highlighted in that speech, which I would like to submit for the record, we are clearly entering an era in which environmental concerns are having a critical and increasing impact on international relations.

Issues such as stratospheric ozone depletion and global climate change have the potential to affect all nations, and an unprecedented degree of international cooperation is required to adequately address these concerns.

The heightened international awareness of the importance of environmental issues was brought home sharply to me when I headed the U.S. Delegation to the meeting on the environment of the Conference on Security and Cooperation in Europe last October 16th through November 3rd in Sofia, Bulgaria.

The degree of consensus among the 35 member states, including virtually every country in eastern and western Europe, as well as the United States, the Soviet Union, and Canada, was remarkable.

Our environmental experts had very fruitful discussions and agreed on constructive action proposals on the three environmental agenda items under consideration, which were transboundary effects of industrial accidents; hazardous chemicals; and transboundary waterways.

DEPARTMENT OF STATE'S ENVIRONMENTAL ACTIVITIES

The Secretary of State's responsibility for exercising the President's foreign affairs powers on a day to day basis gives the Department a central role in developing and implementing U.S. policies on global environmental issues.

Other executive agencies bring extensive scientific, regulatory and other specialized knowledge to our considerations.

The State Department, however, takes the lead in integrating our approach to these issues at the international level, addressing their impact on the community of nations, and coordinating our contribution to the international effort.

To deal with the growing number of international environmental concerns, the Department has devoted significant resources to the environment and to the related areas of science and technology.

During fiscal year 1989, the Department employed 154 full time civil service and foreign service employees in the OES Bureau and an additional 34 full time science and technology officers and fisheries attaches at 25 missions worldwide.

In addition, the number of OES officers dealing specifically with the environment has been increased by almost 30 percent over the past year, primarily through the establishment of a new office to deal with the vital issue of global climate change.

We have also recently set up within the foreign service a separate occupational category for science and technology officers, an important part of whose duties is dealing with environmental issues.

Its establishment has led to expanded promotion, training and assignment prospects for foreign service officers who choose to devote a substantial portion of their career to this important work.

This emphasis on the environment reflects the growing importance of these concerns in our work. Among the issues which will require our increased attention in the decades to come is the serious potential threat of global warming as a result of human activities.

We have been working actively through the Inter-Governmental Panel on Climate Change, so-called IPCC, to develop a sound international approach for dealing with this complex issue.

The IPCC is scheduled to complete an important report this fall assessing our knowledge of the scientific aspects of this issue and providing options for limiting or adapting to climate change.

As reflected in President Bush's address of February 5th to the IPCC, we expect international negotiations on the frame work convention on climate change will begin soon after completion of the IPCC's report.

In addition, in support of the IPCC's efforts, the White House is holding a conference on science and economics research related to global change April 17th and 18th, to which top level environmental, economic and scientific officials from 17 countries have been invited.

U.S. leadership has been similarly evident in negotiations on protection of the stratospheric ozone layer. The United States played a leading role in shaping the historic Montreal Protocol on substances that deplete the ozone layer in 1987, and we are now coordinating U.S. efforts to implement President Bush's call last March for the elimination of chloroflourocarbons by the year 2000, provided that safe substitutes can be found.

We expect to achieve agreement to phase out CFCs at the meeting of the parties of the Montreal Protocol in London in June.

The recent historic events in eastern Europe have also provided a new challenge and opportunity for international environmental cooperation.

To help the eastern Europeans help themselves in the crucial areas of environmental protection and restoration, we are offering our considerable domestic experience.

For instance, we are providing clean coal technology to Poland to help deal with the serious pollution problems in Krakow and for the region as a whole.

We are working to establish the Budapest Regional Environmental Center as first announced by the President last July.

These are only a few examples of the many environmental issues which the State Department is addressing. I have not mentioned, for example, our work within the Convention on International Trade and Endangered Species—the so-called CITES convention, to save the African elephant and other species, or our broad support for the U.N. Environment Program, UNEP, which plays an important role in the negotiation and implementation of a number of international agreements.

We're engaged in numerous multilateral talks on a range of major environmental problems. In summary, Mr. Chairman, international environmental issues will clearly be increasingly important in our diplomatic efforts in the decades to come.

We look forward to working closely with this committee and the Congress as we address our joint objective of protecting the global environment.

Thank you.

[The prepared statement of Mr. Smith follows:]

TESTIMONY OF

RICHARD J. SMITH

ACTING DEPUTY ASSISTANT SECRETARY FOR
ENVIRONMENT, HEALTH, AND NATURAL RESOURCES

BUREAU OF OCEANS AND INTERNATIONAL
ENVIRONMENTAL AND SCIENTIFIC AFFAIRS

DEPARTMENT OF STATE

APRIL 3, 1990

Mr. Chairman, Members of the Committee:

Good morning - I am Richard J. Smith, Acting Deputy Assistant Secretary for Environment, Health, and Natural Resources and Ambassador for Special Negotiations for acid rain with Canada. Having spent the past five years dealing with international environmental and scientific issues, I welcome the opportunity today to talk about global environmental affairs.

Growing Importance of International Environmental Issues

In his recent presentation on our international environmental policy to the National Governors Association, which I would like to submit for the record, Secretary Baker said "environmental threats respect no border." As highlighted in that speech, we are clearly entering an era in which environmental concerns are having a critical and increasing impact on international relations.

Issues such as stratospheric ozone depletion and global climate change have the potential to affect all nations and individuals. Consequently, an unprecedented degree of international cooperation is required to adequately address these new concerns.

During the past year, we have seen environmental issues raised to the highest political levels. At the Paris Summit last July, for example, the leaders of the world's industrialized democracies agreed that concerted efforts were required to safeguard the world environment. They called for "decisive action" to understand and to protect the earth's ecological balance in order to meet economic and social objectives. More than one-third of the final summit communique was devoted to the environment.

Globally, there is a growing awareness of the need for enhanced environmental protection. In Eastern Europe, in the wake of growing health problems and disasters such as Chernobyl, we see clearly the belated recognition of the need to reconcile environmental protection and industrial development. The less developed countries are likewise becoming aware of the need to ensure that their economic growth is environmentally sustainable.

This heightened international awareness of the importance of the environment was brought home sharply to me when I headed the U.S. delegation to the Conference on Security and Cooperation in Europe (CSCE) meeting on the environment in Sofia, Bulgaria last October 16-November 3. The degree of consensus among the 35 member states, including virtually every country in East and West Europe as well as the United States and Canada, was remarkable. Our environmental experts had very fruitful discussions and agreed on constructive action proposals on the three environmental agenda items under consideration: transboundary effects of industrial accidents; hazardous chemicals; and transboundary waterways.

State Department Role in International Environmental Policy

The Secretary of State's responsibility for exercising the President's foreign affairs powers on a day-to-day basis gives the Department a central role in developing and implementing U.S. policies on these increasingly global environmental issues. Other executive agencies bring extensive scientific, regulatory and other specialized knowledge of environmental issues to our consideration. The State Department, however, takes the lead in integrating our approach to these issues at the international level, assessing their impact on the community of nations, and coordinating our contribution to the international effort to address these issues in the most effective and economical manner.

The Congress long ago recognized the importance of this integrative function and in 1973 created for this purpose the Bureau of Oceans and International Environmental and Scientific Affairs (OES) within the Department of State. In addition, the specific authority of the Secretary of State to oversee and coordinate not only bilateral and multilateral environmental issues, but also the full range of international scientific and technological affairs, has been recognized on numerous occasions, including, for example, in the State Department Appropriation Act of 1979.

To deal with the increased importance and growing number of international environmental concerns, the Department has devoted significant resources to the environment and to the related areas of science and technology. During FY-1989 the Department employed 154 full-time civil service and foreign service employees in the OES Bureau, and an additional 34 full-time science and technology officers and fisheries attaches at 25 missions worldwide.

We have also recently established within the Foreign Service a separate occupational category for science and technology officers whose duties include dealing with environmental issues. Its establishment has led to expanded promotion, training and assignment prospects for Foreign Service officers who choose to devote a substantial portion of their career to this important work.

In addition, the OES Bureau has established a new Office of Global Change greatly enhancing our ability to deal with the vital issue of global climate change.

The Department's expanding role reflects the the increasing emphasis on environmental problems in our foreign policy. The United States is presently engaged in some 20 major environmental negotiations, including talks related to climate change, conservation of ocean resources, pollution abatement, and the protection of biodiversity. In addition, the Department coordinates and oversees implementation of several hundred science and technology agreements with foreign countries, many of which provide for important joint progress in environment related research.

Major Ongoing International Environmental Negotiations

The Department of State is actively involved at this time in a number of major international negotiations on the environment. Among the most important issues we face is the potential threat of climate change as a result of human activities. Recognizing the need for a mechanism to focus international efforts on this complex issue, the United States strongly supported the establishment, under the auspices of the World Meteorological Organization (WMO) and the United Nations Environment Program (UNEP), of the Intergovernmental Panel on

Climate Change, which has become the primary international forum for addressing all aspects of the climate change issue.

The IPCC is scheduled to complete an important report this fall assessing our knowledge of the scientific aspects of this issue and providing options for limiting or adapting to climate change. We expect international negotiations on a framework convention on climate change will begin soon after completion of the IPCC's report. In his address to the IPCC last February, the President highlighted the U.S. commitment to addressing climate change and offered the United States as the venue for the first round of negotiations on the framework convention.

U.S. leadership was similarly evident in the negotiations leading to the signing of the Montreal Protocol on Substances that Deplete the Ozone Layer in 1987. The United States played a leading role in shaping this historic Protocol, which called for reduction of chloroflourocarbons (CFCs) to 50 percent of 1986 levels by 1998, and we continue to be active in its implementation. Because our understanding of the effect of chloroflourocarbons on the stratospheric ozone has advanced considerably since 1987, the President last March expressed his recognition that the reduction of CFCs called for in the Montreal Protocol may not be enough, and he called for the elimination of CFCs by the year 2000, provided that safe substitutes are available. We are now coordinating U.S. efforts through the assessment process provided for by the Montreal Protocol to implement the President's mandate on an international basis. We expect to achieve agreement to phase out CFCs at the Meeting of the Parties to the Montreal Protocol in London in June.

The recent historic events in Eastern Europe have provided a new challenge and opportunity for international environmental cooperation. To help the East Europeans help themselves in the crucial areas of the environmental protection and restoration, we are offering our considerable domestic experience in dealing with these issues. For instance, we are providing clean-coal technology to Poland, to help deal with the serious pollution problems in Krakow, which are ruining that city's historic architectural treasures. For the region as a whole, we are working, along with A.I.D. and EPA, to establish the Budapest Regional Environmental Center, first announced by President Bush last July.

We are also working under science and technology agreements with Yugoslavia, Hungary, Poland and Czechoslovakia to expand our cooperation on environmental matters. However, I must note that at the present time the Department is enjoined by Section 614 of the Departments of Commerce, Justice, and State, the Judiciary and Related Agencies Appropriations Act of FY 1990 from spending above FY 1989 levels - this limitation could seriously impact on our science and technology programs and our foreign policy objectives in Eastern Europe.

We have also acted vigorously to protect endangered species through the Convention on International Trade in Endangered Species of Wild Fauna and Flora (CITES). CITES has been particularly crucial to our efforts to protect the drastically declining populations of the African elephant. I am pleased to note that, with strong U.S. support, CITES in October 1989 decided to halt the international trade in elephant ivory, which had been identified as one of the main causes of the elephant populations' decline.

These are only a few examples of the many environmental issues which the State Department is addressing. I have not mentioned, for example, our broad support for the U.N. Environment Program (UNEP), which plays an important role in the negotiation and implementation of a number of international agreements. We are also becoming increasingly active within the UN Econmic Commission for Europe (ECE) which is playing more and more of a leadership role on environmental issues. Also, we are currently undertaking efforts towards becoming a governmental member of the International Union for the Conservation of Nature and Natural Resources (IUCN) and expect to do so by the end of the year.

International environmental issues will clearly be increasingly important in our diplomatic efforts in the decades to come. Furthermore, based on past experience, we can be sure that the coming decade will produce unexpected challenges and I have no doubt that we will have to face many difficult choices as we decide how and where to best apply our resources in the future. We look forward to working closely with this committee and the Congress as we address our joint objective of dealing effectively with these vital global environmental issues.

Secretary Baker

Current
Policy
No. 1254

Diplomacy for the Environment

United States Department of State
Bureau of Public Affairs
Washington, D.C.

Following is an address by Secretary Baker before the National Governors Association, February 26, 1990, Washington, D.C.

I'm pleased to have this opportunity to talk to you today about the environment. It is a subject that is important to me personally and also very important for the 50 states, the territories, and for our foreign policy.

A little history may be in order. In 1852, Chief Seattle responded to a request of the U.S. Government to purchase some tribal lands for the arriving pioneers. The chief replied: "The Earth does not belong to man, man belongs to the Earth. All things are connected like the blood that unites us all: man did not weave the web of life, he is merely a strand in it." And the chief warned, "Whatever he does to the web, he does to himself."

The settlers kept moving West—my great-grandfather among them. These independent, hard-working, and courageous people helped to make our great nation what it is today. Even for those of us whose ancestors did not take part in the westward saga, the pioneers still epitomize the essence of the American spirit.

Yet, by century's close, it had already become evident to many Americans—from the developed East and the developing West alike—that America's bounty was not inexhaustible. It had become apparent that we needed to take responsibility for protecting and replenishing our natural resources so that future generations could enjoy them.

In 1908 at the White House, President Theodore Roosevelt convened a conference on the conservation of natural resources—the first of its kind not only in the United States, but in the world. It was known as the Conference of Governors. And it is fair to say that the conference was the single greatest stimulus to the creation of a responsible national environmental policy for the United States.

Now, as we plan ahead for the next century, we must remember the lessons of the 19th and the 20th centuries.

From America's native peoples, we have learned that we cannot take nature for granted. We must cherish it and respect its God-given dignity.

From our forefathers, we have learned that nature is not a cornucopia of unending supply. We must give back to the Earth if we are to continue to draw from it.

From the history of the conservation movement in the United States, we have learned that state and federal governments, business and labor, national organizations, and individual citizens must work together if we are to craft effective environmental policies.

Finally, we know from our own experience in this interdependent world that we must "think local and act global." We cannot serve America's environmental interests effectively unless we address worldwide environmental concerns. That is where foreign policy enters the picture. And that's what I'd like to talk about today.

The Environment and U.S. Foreign Policy

The foreign policy objectives of the United States are grounded in our basic values. We seek to encourage democracy, foster prosperity through economic liberty, ensure security, and improve effective international cooperation that addresses our common interests. What is not well-known, however, is that our environmental concerns have a major role to play in the achievement of each of these objectives: democracy, prosperity, security, cooperation, the environment—they are all interconnected. That is why the President and I are committed to ensuring that environmental issues are fully integrated into our diplomatic efforts. This is the greening of our foreign policy.

Democracy and the Environment

So first, I would like to discuss how our efforts to consolidate democracy are linked to our environmental efforts. Democracies—dependent as they are on an informed citizenry, an open society, and accountability in government—afford the greatest scope for responsible environmental action. The conservation movement is one of the greatest success stories for grassroots democracy in the United States. When we defend and promote democratic and environmental values, we express the essence of what we believe is essential for all nations to make progress—developed and developing nations alike.

Let me give you a vivid example of how democrats and environmentalists make common cause. In Eastern Europe, environmental concerns were championed by democratic opposition groups long before the people power revolutions of last fall. In fact, environmental issues helped galvanize the push for democracy. It was an international environmental conference in Sofia, Bulgaria, which helped to spark the popular revolution. "The Ecoglasnost Association," formed in anticipation of that conference, is now one of Bulgaria's largest grassroots organizations and democratic opposition groups. So in Bulgaria, Ecoglasnost gave the term "Green Revolution" a whole new meaning.

The environment is clearly one of those points of mutual advantage between East and West that the President and I are pledged to seek as we try to leave the cold war behind. To help the East Europeans help themselves in the crucial area of environment, we are offering our whole experience in dealing with these issues. We are offering to the emerging democracies grants and concessional loans; joint projects, training and technology; as well as guidance in drafting laws and regulations.

For instance, we have proposed a joint U.S.-Czechoslovak study to determine the most cost-effective way to deal with Czechoslovakia's serious air pollution problems. We are providing clean-coal technology to Poland, in part to arrest the tragic defacement of Krakow's historic architectural treasures—treasures literally being eaten away, day by day. For the region as a whole, we have promoted participation in the Budapest Regional Environmental Center, first announced by President Bush last July. With the Soviet Union, Foreign Minister Shevardnadze has agreed to my request to add to our meetings a fifth major agenda item on transnational concerns. Environment is the most prominent issue in these ongoing discussions.

The sum total of all these projects will reinforce the trends toward democracy in the East—that is, governments responsible to the people and the concerns of the people.

That brings us to our second major objective: promoting prosperity and economic liberty. Just as political freedom and economic liberty go hand in hand, so, too, do sustained growth and a healthy environment. Strong economies provide the material means with which to protect the environment. These relationships are symbiotic. They are expressed by the concept called "sustainable development."

Sustainable development, to put it simply, is a way to fulfill the requirements of the present without compromising the future. When policies of sustainable development are followed, our economic and our environmental objectives are both achieved. In fact, America's entire approach to bilateral and multilateral assistance is based on the concept of sustainable development.

Providing market-based incentives, eliminating structural impediments, and ending international trade practices that distort global markets—all will generate an economic dynamism that benefits the developed and developing world alike.

Bilateral and Multilateral Efforts

Let me cite a few examples of how we are making the concept of sustain-able development work through our bilateral assistance efforts. In Rwanda, we are sponsoring a project linking the economic benefits of tourism with the conservation of two unique, species-rich protected areas. In other developing countries around the world, we are fostering biodiversity. By so doing, we can increase the availability of natural products for commercial purposes. Life-saving pharmaceuticals and other marketable goods such as food and dyes can result. An ongoing AID [Agency for International Development] project in Indonesia focuses on the management and conservation of exotic native fruits, which may prove marketable. This project also promotes the management practices needed to stem the wanton destruction of tropical forests.

Innovative efforts, such as debt-for-nature swaps, are also important. These, like all other debt reduction efforts, must involve basic structural reform if they are to succeed. Debt swaps are not the panacea for debt reduction, nor can they single-handedly solve environmental problems, but debt swaps can help with both.

On the multilateral level, the development banks can play a key role in promoting environmentally sustainable growth. We will continue to encourage the multilateral development banks to strengthen their policies, staff, and training. We hope other donor countries will join our efforts to integrate environmental assessments into all operations of the development banks.

I know that there are dramatic calls by some for the establishment of new financial institutions or mechanisms to provide environmental assistance. But before we spend our scarce resources on creating new bureaucracies, it makes good sense to make maximum use of the multilateral tools already in existence and to reinforce existing institutions.

Similarly, before we dedicate additional resources toward international environmental efforts, we will need to know how much is required. Substantial funding for environmental projects is already available. We fully recognize, however, that developing countries may need some additional aid in order to meet the incremental costs associated with fulfilling their international environmental obligations.

Our third key objective is ensuring global security. Solid democracies and sound economies cannot grow in unsafe surroundings. We have long worked in partnership with friendly nations to protect ourselves against traditional security threats from hostile governments. But in today's world, traditional concepts of threats to the security of our citizens need to be updated and extended to include the new transnational dangers—environmental degradation among them.

Environmental Threats Are Everyone's Concern

Environmental threats respect no border. They threaten human lives and violate the territorial integrity of states from both within and without. Chernobyl—a classic example of the ills of the stagnant Brezhnev era—showed how lives can be needlessly endangered when governments fail to act quickly and responsibly to protect their own citizens and the people of neighboring countries.

Not surprisingly, the drug cartels that threaten the health of the world community also damage the environment. As I pointed out at the UN Special Session on Narcotics last week, traffickers in the Andes are destroying vast tracts of forest for their drug labs and are dumping millions of gallons of precursor chemicals into rivers.

Forty years ago, we and our NATO partners pledged to "safeguard the common heritage and civilization" of Europe against our common enemies. As the President pointed out, Europe's environment is the common heritage of all Europeans, and we all must work to protect it. As we have seen, defending Europe's environment from the threat of pollution is just another way for the West to help the peoples of the East realize their dream of a Europe whole and free.

Our fourth objective is enhancing effective international cooperation that addresses our common interests. As we have seen, many of today's problems—environmental problems especially—have worldwide consequences. They demand global solutions. All nations share responsibility for the protection of the international community.

No nation alone, however great, can dictate fully the course of human events nor fully protect its natural resources. And no nation, however small, is without the power to act for the health of the global community. All countries must act responsibly and work together.

I am glad to say that more than ever before, nations all over the world are working together on global environmental problems. Let me give you two examples. One is global climate change. Just a few weeks ago, the President addressed the Intergovernmental Panel on Climate Change. He was the first head of state to speak before the panel. And his presence demonstrated the seriousness with which our government regards this question as well as our dedication to finding appropriate scientific, economic, and environmental solutions. The President reiterated our policy toward climate change. We call it the "no regrets" policy, and we encourage other nations to adopt a similar approach.

Just what do we mean by "no regrets"? We mean that while we are pursuing the serious scientific research that is critical to any responsible approach, we're also hedging our bets in an economically sound way. We mean that the United States is making a major financial commitment to analyze these scientific issues, increasing our funding for the U.S. Global Change Research Program to over $1 billion. And we mean that we are prepared to take actions that are fully justified in their own right and which have the added advantage of coping with greenhouse gases. They're precisely the policies we will never have cause to regret. Specifically:

- We are committed to phasing out chlorofluorocarbons (CFCs) by the year 2000 to protect the ozone layer. CFCs also contribute significantly to the "greenhouse" effect.

- Next, the President has launched a major reforestation initiative called "America the Beautiful." Under this multiyear program, our citizens will plant 1 billion trees each year in partnership with the government and busines. The trees will provide habitats for wildlife, stem soil erosion, provide recreational facilities, offer employment, and generate forest products. At the same time, the trees will help absorb carbon dioxide, a major "greenhouse" gas.

- Finally, we are dedicated to a program of energy conservation and energy efficiency. This contributes to efficient use of scarce energy supplies, reduces our dependence on foreign energy sources, and saves us all money —citizens, government, and industry alike. Moreover, decreasing the use of the fossil fuels will reduce "greenhouse" gas emissions.

If the results of international scientific research demonstrate that climatic conditions will not change in a significant way, we will have "no regrets" for these actions because they provided other benefits. If, on the other hand, the findings of our research turn out to be more troublesome, we will have taken prudent steps toward solving the problem in a cost-effective way. We urge other nations to join us in our "no regrets" efforts.

A final example of global cooperation involves a denizen of the animal family—a party animal. Some might say he is a partisan creature, but he has bipartisan virtues. Sadly, he is listed among the severely endangered species. Even the Democrats among us agree that if we let our old friend the elephant pass from the earth, we will all be diminished. Therefore, last summer the United States led the way in banning the international trade in ivory. Now, a global effort is underway. Most other nations have joined us. And although some trading in ivory continues, I believe we can all work together to develop an enforcement system that saves the African elephant.

Conclusion

The environmental efforts that I have described here today are illustrative of the many ways the Bush Administration is acting to protect the environment nationally and internationally. This morning, I have not even begun to touch upon our no-net-loss of wetlands policy, our opening of formal discussions with Canada on acid rain, or our driftnet resolution that was adopted unanimously by the United Nations. Nor have I touched upon another major environmental initiative of this Administration: crafting a revised Clean Air Act with incentives for our private sector to find creative, market-driven solutions to enhance air quality. And I am very hopeful that we will soon be able to sign the Basel convention, which controls exports of hazardous wastes.

The United States is doing all of these things because it serves our national interest to do them. We are also doing them because they are fundamentally the right thing to do. The great early pioneers of American conservation recognized these truths, and they found effective ways to act upon them. Their views didn't always prevail with the officials of their era, and they certainly didn't always agree with one another. Controversies that raged around the Governor's Conference back in 1908 continue down to this day. Indeed, environmental issues have never been simple; they never will be. Environmental problems are complex and sometimes slow to develop. And sometimes, we are even slower to recognize them.

Yet despite the intense debates, despite all the uncertainties, despite the sheer complexities involved, there remains before us, as before all peoples, the unquestioned responsibility to act. Emerson, the 19th century American essayist and poet, put it this way: "We do not inherit the Earth from our ancestors, we borrow it from our children."

This is a sacred debt that must be honored. The splendor of nature enfolds and unites all of humankind. Now, together, the earth's peoples must work, so that this precious web of life shall embrace, in beauty and in peace, all the generations to come. ■

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Mr. OBEY. Thank you.

Mr. Vukmanic?

MR. VUKMANIC'S OPENING STATEMENT

Mr. VUKMANIC. Thank you very much, Mr. Chairman.

I am pleased to participate in this panel on environmental issues. As you are fully aware, the Treasury and the Administration has an extensive mandate from the Congress directing us to seek more than 30 specific environmental reforms in the multilateral development banks.

We believe we've made a very concerted and conscientious effort to carry out this mandate, and we have some success to report in these areas.

What I'd like to do is cover five areas very quickly, which are covered in more detail in my statement, the first being administrative issues in this area; the second being general progress that has occurred in the MDBs; the third, the tropical forest area and protection of tropical forests; fourth, energy efficiency and conservation; and the fifth, debt for nature swaps.

ADMINISTRATION'S ENVIRONMENTAL INITIATIVES

With regard to administrative initiatives, I think we can indicate that we've tried every venue and opportunity to raise these issues at the highest levels, as well as at other levels such as negotiations.

At last year's economic summit, the President raised with other heads of State the issue of environment and encouraged them to integrate into the operations of the multilateral development bank environmental considerations.

He also raised these issues at the annual meetings of the World Bank and the International Monetary Fund and encouraged other countries to weigh environmental considerations more heavily in their economic decision making and to work more cooperatively together to develop a constructive response to global warming.

The President specifically emphasized measures to promote energy efficiency and conservation and greater protection of tropical forests.

The Treasury certainly has pursued the full range of environmental reforms in all the international meetings that we have had an opportunity to raise these issues at.

Certainly, at the Interim and Development Committee meetings, the annual meetings of the Bank and the Fund, and the OECD ministerial meetings these issues have been raised, and also we take the occasion of all of the annual meetings of the regional banks to emphasize the importance of taking into account environmental activities.

These reform issues are, I think in a most important sense, taken up at the point of replenishments or capital increases in the banks, and we've already heard several panelists indicate that during the ninth replenishment of IDA, we saw and achieved fairly substantial reforms in the operations of that agency.

Most recently, also in the Inter-American Development Bank negotiations, and certainly in the negotiations now ongoing of the European Bank for Reconstruction and Development.

In IDA, if I may digress a bit, I'd like to point out areas where we've made some fairly significant strides. The agreement for IDA-9 provides for the implementation of environmental impact assessment procedures.

It also provides for increasing public access to environmental information, including environmental impact assessments or summaries of them.

It provides for closer collaboration and cooperation with non-governmental organizations in borrowing countries, with greater emphasis on energy efficiency and conservation, including end use efficiencies, renewable energy technologies and least cost planning in borrowing countries.

It provides for more support for debt for nature swaps and more rapid progress on environmental action plans. In fact, environmental action plans are to be completed for all IDA borrowers as quickly as possible.

MDB PROGRESS ON THE ENVIRONMENT

Now, with regard to the MDBs in general, I've got quite a bit I could report in terms of progress, and let me just sort of summarize.

I think in all of the MDBs we've seen an increase in staff. Certainly, in some, the World Bank and the IDB, the staff increase has been more dramatic than in others.

In the African Development Bank, we continue to have problems with regard to staff, and we are trying to address those problems by seconding professionals to the bank.

In all the banks, we have impressed upon them and put pressure on them to increase their coordination and collaboration with NGOs. I think we see that is occurring. As I indicated, in the IDA-9 agreement, certainly in the Asian Development Bank, that has improved dramatically, moving all the way down to the beginning stages of project development. And in the IDB we've seen a significant improvement in NGO coordination.

In the African Development Bank, we have NGO coordination being improved by several NGO groups in the United States taking a very active role in developing a coordination process through seminars, et cetera, with the bank, which we have also encouraged.

In all the banks also we've seen an increase in environmentally beneficial lending and just a general emphasis on this area. As I said, there is much more detail in my written statement, and I'll forego repeating that now.

TROPICAL FOREST PROTECTION, DEBT SWAPS, AND ENERGY CONSERVATION

In the third area, the protection of tropical forests, this subcommittee had a particular interest and passed legislation last year emphasizing programs for the protection of these forests.

This is an area that we have monitored very closely and an area that is a very strong concern to the Treasury.

In 1988, we adopted standards for the evaluation of loans in the MDBs that might adversely affect moist tropical forests. At our urging, the World Bank has announced plans to adopt its own tropical forest standards which we hope and expect will be announced and put into place later this year.

The Administration has also supported the work of the Tropical Forestry Action Plan. The plan, led by the World Bank, the Food and Agricultural Organization and the United Nations Development Program, seeks to provide an overall frame work for preserving and replenishing tropical forest resources in developing countries and undertakes forestry sector reviews, and identifies specific projects that both bilateral and multilateral donors can fund.

We believe the TFAP is the correct conceptual approach in addressing this important area. We have problems, however, with specific loans under the Tropical Forest Action Plan program.

We believe there should be a better balance between timber programs and the preservation and protection elements of individual loans.

We also believe that the TFAP process has been too closed a process. It excludes, in many cases, the participation of forest dwellers and NGOs.

So what we've been encouraging is for the program to put greater emphasis on strengthening institutional capacities for park management, for forestry preservation in borrowing countries, and for the involvement of non-governmental organizations in all stages of planning and implementation.

We're working with NGOs such as the World Wildlife Fund to try and strengthen this process and to evaluate specific loan proposals coming out from it.

In the area of debt for nature swaps, which we had some discussion of by earlier participants, as you know, Treasury encouraged the World Bank to become more active in this area. I must report, unfortunately, that the progress has been extremely slow.

We are encouraged by a recent proposal to preserve a very large tract of Atlantic Rain Forest in Paraguay, something in the order of 69,000 hectares of virgin, humid, semi-tropical rain forest. This rain forest is the last large privately owned tract of this unique vegetation type in Latin America.

The IFC, the International Finance Corporation, is working with A.I.D. and The Nature Conservancy to transfer title to an appropriate Paraguayan institution and to establish a nature reserve in the area.

We understand that A.I.D. is prepared to provide $500,000 for the proposal and that The Nature Conservancy and other private organizations would provide the remainder of the funding.

Although the agreement on this debt for nature swap is not assured, we certainly hope that it comes to fruition, and we expect and hope that it will be a model for future debt for nature transactions.

In the area of energy efficiency and conservation, we know that is another important area for the subcommittee. During the past year, the Treasury has worked to form an informal working group comprised of experts from U.S.A.I.D., the Environmental Protection Agency, the Departments of State and Energy, and several NGOs to exchange views on how we might encourage greater emphasis on energy efficiency and conservation in the MDBs.

Much of the specificity that we were able to achieve in the IDA-9 negotiations came out of this group's work. The Treasury is also an active member on the Committee of Renewable Energy in Commerce and Trade, CORECT.

We helped draft a financing paper for CORECT emphasizing the role of the World Bank and encouraging this process. The bank is now working with the Department of Energy to identify and help implement innovative mechanisms for financing renewable energy and conservation services for small energy consumers in developing countries.

This project, financing of energy services for small scale energy users—sorry for the acronym, FINES is being targeted initially for the southeast Asian countries, Indonesia, Malaysia, the Philippines, and Thailand.

Let me skip a bit and just say we're also looking——

Mr. OBEY. If I could ask you to summarize, because you guys are filibustering me right out of any time for questions.

Mr. VUKMANIC. I apologize for that. Let me just say that the bank is working, as I indicated, with small enterprises, the bank is also working through ESMAP to develop proposals on projects in this area, and I'll just stop there.

[The prepared statement of Mr. Vukmanic follows:]

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STATEMENT OF FRANK VUKMANIC
DIRECTOR OF THE OFFICE OF
MULTILATERAL DEVELOPMENT BANKS
DEPARTMENT OF THE TREASURY
BEFORE THE SUBCOMMITTEE ON FOREIGN OPERATIONS
COMMITTEE ON APPROPRIATIONS
U.S. HOUSE OF REPRESENTATIVES

Introduction:

Mr. Chairman: I am pleased to participate in this panel on global environmental issues and international economic assistance programs. My statement today will report on several initiatives that Treasury has taken within the Multilateral Development Banks over the past year and how we have sought to shape the policies of those institutions in this increasingly important area.

We have received an extensive mandate from Congress directing us to seek more than thirty specific environmental reforms in the Multilateral Development Banks. These reforms have included: restructuring and strengthening of environmental line units; hiring of environmentally-qualified staff; greater emphasis on staff training on environmental implications of development; increased coordination with local community groups and non-governmental organizations; and the preparation of additional projects that will have a positive and beneficial effect on the environment. We have made a concerted and conscientious effort to carry out this mandate and I believe we have some substantial successes to report.

Administration Initiatives:

At last year's Economic Summit meeting in Paris in July, President Bush asked other heads of state and government to join him in encouraging the World Bank and the regional development banks to integrate environmental considerations into all aspects of their activities. At the Annual Meetings of the World Bank and International Monetary Fund last September, the President encouraged other countries to weigh environmental considerations more heavily in economic decision-making, and said that we need to work more cooperatively together to develop constructive responses to global warming, specifically emphasizing measures to promote energy efficiency and conservation and greater protection of tropical forests.

Treasury has pursued the full range of environmental reform issues in numerous international meetings: meetings of the Development Committee of the World Bank and IMF in April 1989 and in September 1989, the Annual Meetings of the World Bank and IMF last September, and the ministerial meeting of the Organization for Economic Cooperation and Development last May. In addition, we have emphasized the importance of environmental reforms in the annual meetings of the three regional banks. Such reform issues have been an important part of U.S. negotiations to replenish the resources of these institutions, particularly those of the Inter-American Development Bank (IDB) and the ninth replenishment of the International Development Association (IDA-9). We have also raised environmental issues in the negotiations now going forward for establishment of the European Bank for Reconstruction and Development (EBRD).

IDA Replenishment:

One of our most significant accomplishments in the IDA-9 negotiations was the inclusion of more stringent environmental provisions in the replenishment agreement. That agreement provides for:

-- Implementation of environmental impact assessment (EIA) procedures, thereby helping to assure that environmental costs and benefits are weighed carefully early in the project appraisal process.

    - Projects which are expected to have significant environmental consequences will receive rigorous technical reviews at sufficiently early stages of project preparation to ensure that their environmental impacts are fully factored into decisions on site selection and project design.

    - As part of this process, environmental impact assessments will be made available to the Executive Board at least 180 days in advance of Board action;

-- Increasing public access to environmental information, including environmental impact assessments or summaries of them, thereby promoting participation by local community groups and non-governmental organizations;

-- Closer collaboration and cooperation with non-governmental organizations in borrowing countries;

-- Greater emphasis on energy efficiency and conservation, including end-use efficiencies, renewable energy technologies, and least-cost planning in borrowing countries;

-- More support for debt for nature swaps; and

-- More rapid progress on environmental action plans. Environmental action plans will be completed on all IDA borrowers as soon as feasible.

Progress within the Banks:

A great deal has already been accomplished on a number of environmental reforms within the Multilateral Development Banks. Let me cite some specific examples that will illustrate the progress that has been made over the past year. At last count, the World Bank had approximately 100 individuals working on various aspects of environmental issues. This is up from approximately 65 individuals a year ago. Last September, the Bank adopted an operational directive for assuring that environmental impact assessments are completed for projects that will have a significant effect on the environment.

In January, the Inter-American Development Bank established an environmental line unit and assigned fifteen professionals to carry out the functions of the unit. In February, the Bank adopted environmental classification and impact assessment procedures. It has also continued its work with non-governmental organizations and local community groups, sponsoring a conference on environmental issues in the hemisphere last year and inviting many organizations and groups from borrowing member countries to participate.

The Asian Development Bank has continued its efforts to integrate environmental considerations more effectively into the project appraisal process -- setting up a comprehensive review system that produces environment reports on specific projects at six stages of the appraisal progress. The Bank has also sought to involve non-governmental organizations from developing countries in identification and preparation of specific project proposals. Projects that have benefited from this NGO involvement include two from the Philippines, one from Nepal and one from Bangladesh. In June, 1989, the ADB also sponsored a consultative meeting with non-governmental organizations from the region. It is pursuing other work on NGO institutions and capabilities and a study on the possibilities for debt for nature swaps.

The African Development Bank has been working closely with three U.S. non-governmental organizations -- the Sierra Club, the Natural Resources Defense Council, and the American

Farm Trust -- to increase its cooperation and coordination with non-governmental organizations in Africa. An initial meeting -- involving a number of African organizations -- was held last September in Abidjan. We have encouraged this process and hope that the U.S. organizations will be able to continue their activities in this area. The African Development Bank has also developed an environmental policy paper to guide its lending activities as they affect the environment. The paper is currently under review by a committee of the board of executive directors of the Bank.

All of the Multilateral Development Banks are reporting continuing increases in the number of environmentally beneficial projects and of projects with environmentally beneficial components. There has also been a rapid rise in technical assistance programs for preparation of environmentally beneficial projects and strengthening of environmental institutions in borrowing countries.

We are pleased with the progress achieved thus far. At the same time, we recognize there is much more that remains to be done. We will encourage the Asian Development Bank and the African Development Bank to increase the number of environmentally-qualified staff. We will continue the emphasis we have already placed on energy efficiency and conservation measures and programs to protect tropical forests. We will increase our efforts to assure that the agreements we have reached are implemented effectively.

In the World Bank, implementation of environmental impact assessment procedures over the next two years will be a difficult and time-consuming task. We are consulting with Department of State, USAID, the Environmental Protection Agency, and the Council on Environmental Quality about the possibility of detailing U.S. experts to assist in this process. We are also asking other countries to consider seconding experts for this purpose as well. In the regional development banks, this task will be even more daunting, and will almost certainly require additional efforts by us and other developed countries.

Protection of Tropical Forests:

In legislation that was passed last year, this subcommittee emphasized the importance of programs for protecting tropical forest resources. This is an area which we have watched closely and one where we have had serious concerns for several years. Members may recall that the Treasury Department in 1988 adopted standards for U.S. evaluation of Multilateral Development Bank projects that may adversely affect tropical moist forests. At our urging, the World Bank announced plans to adopt its own standards for such projects. We expect those standards to be put in place later this year. We hope that they will provide a suitable framework for the Bank's projected increase in lending for tropical forestry projects.

The Administration has also supported the work of the Tropical Forestry Action Plan (TFAP). This Plan, led by the World Bank, the Food and Agriculture Organization and the United Nations Development Program, seeks to provide an overall framework -- institutional, policy and loan strategy -- for preserving and replenishing tropical forest resources in developing countries. It undertakes forestry sector reviews in individual countries and identifies specific projects that may be funded by both bilateral and multilateral donors.

We believe that the conceptional approach being taken TFAP is correct. However, we have encountered some problems with the development of specific loans under the TFAP program. In particular, we are concerned that there be a better balance between timber programs and the preservation and protection elements of individual loans. In many cases, the TFAP process has also been too much of a closed process, excluding the participation of forest dwellers and NGOs. Accordingly, we have encouraged reforming and strengthening of TFAP programs, urging greater emphasis on building up institutional capacities for park management and forestry preservation in borrowing countries and involving non-governmental organizations in all stages of planning and implementation.

We are working closely with non-governmental organizations such as World Wildlife Fund in this area. We are also working closely with these organizations on evaluating specific MDB loan proposals that may present problems. In June of 1989, we were successful in making changes in a forestry loan to Sri Lanka from the World Bank. In December, we undertook a particularly close review of a $8 million forestry project in Guinea, urging the World Bank to put more weight on protection and preservation elements in the loan. We are now conducting an even more searching review of an $80 million loan to Ivory Coast because of similar concerns.

Debt for Nature Swaps:

In 1988, Treasury encouraged the World Bank Group to play a more active role in promoting debt for nature swaps. Unfortunately, progress in this area has not been as rapid as we had first hoped. One recent encouraging sign has been a proposal to preserve an important tract of Atlantic rain forest in Paraguay. The tract extends over 69,000 hectares and is a virgin, humid, semitropical rainforest of particularly rich biodiversity. It is the last large privately-owned tract of this unique vegetation type in Latin America.

The International Finance Corporation, which acquired the tract a number of years ago through foreclosure, is working with USAID and Nature Conservancy to transfer title to an appropriate Paraguayan institution and establish a nature reserve in the area. The parties are also seeking to finance the recurrent costs associated with reserve management. Our understanding is that USAID is willing to provide $500,000 for the proposal and that other funding would come from Nature Conservancy and other private organizations. Although an agreement is not assured at this time, we are hopeful that the project will go forward under World Bank auspices and that it will be a model for future debt for nature transactions.

Energy Efficiency and Conservation:

Energy efficiency and conservation measures are another important area in which we have received a significant legislative mandate from this sub-committee. During the past year, Treasury formed an informal working group comprised of experts from USAID, the Environmental Protection Agency, the Departments of State and Energy, and several NGOs to exchange views on how we might encourage greater emphasis on energy efficiency and conservation in the Multilateral Development Banks. Much of the specificity that we were able to achieve in the IDA-9 Agreement grew out of the work of this group.

Treasury has also been an active member of the Committee on Renewable Energy, Commerce, and Trade (CORECT), which seeks to encourage greater reliance on renewable energy technologies in developing countries. We have helped to draft a financing paper for the committee emphasizing the role of the World Bank in encouraging this process. The World Bank, itself, is now working with the Department of Energy to identify and help implement innovative mechanisms for financing renewable energy and conservation services for small energy consumers in developing countries. This project, Financing of Energy Services for Small-scale Energy Users, also known as FINESSE, is being targeted initially at four southeast Asian countries --Indonesia, Malaysia, Philippines and Thailand. A workshop is scheduled to be held in Kala Lumpur in the spring of 1991. This week, the World Bank and USAID are sponsoring a seminar on use of wind energy for large scale electric power production.

We have also encouraged the World Bank to work more closely with USAID in developing least-cost energy plans in borrowing countries and in coordinating their overall programs in energy efficiency and conservation. The Energy Section Management Assistance Program (ESMAP) is expected to put more emphasis on integrating the results of their studies and assessments into the capital lending programs of the Bank. A high level review of ESMAP is also underway and more specific recommendations are expected in the near future. In the regional development banks, we are also asking for greater emphasis on renewable energy technologies, end-use efficiencies and least-cost planning.

Conclusion:

Mr. Chairman, I believe we are making good progress on the full range of environmental reforms in all of the Multilateral Development Banks. We have been particularly encouraged by the adoption of procedures for environmental impact assessment in both the World Bank and the Inter-American Development Bank. We look forward to adoption of similar procedures in the other banks. Effective implementation of these procedures will be difficult and time-consuming and require technical support from us and other member countries.

Energy efficiencies and conservation and protection of tropical forests are two other key areas which clearly need additional attention from us. We are making a good start in both of these areas -- in reviewing the Energy Sector Management Assistance Program (ESMAP) in the World Bank and in working to reform and strengthen the mandate of the Tropical Forestry Action Plan (TFAP). We have had important support in these areas from other agencies in the U.S. Government and from non-governmental organizations that are interested in these issues. I am convinced that we will continue to make important progress in the year ahead.

Mr. OBEY. Thank you.

UNEP, GLOBAL WARMING, AND CFCS

Mr. Smith, in your testimony, you indicated the Administration's broad support for the United Nations Environment Program, but the budget request represents a 15 percent cut in our support for that program.

What would the budget look like if the Administration had a narrow support for the United Nations Environment Program?

Mr. SMITH. Well, all I can say on that is that the budget is put together in difficult times when you have to balance priorities.

Mr. OBEY. So we wind up adding $300 million to military aid and cutting the United Nations Environment Program? What does the Administration think of the UNEP?

Mr. SMITH. We think it's an effective organization. We're working with it very intensely, and we are very supportive of what they're doing.

Mr. OBEY. Just not sufficiently supportive to give them what we gave them last year.

Mr. SMITH. I can't really speak to the design of the budget proposal this time, but it was designed to do what we felt was necessary.

Mr. OBEY. Let me ask you about global climate change. A year ago, the Secretary of State, at the first meeting of the IPCC, said we can probably not afford to wait until all of the uncertainties have been resolved. In discussing the issue of global warming, time will not make the problem go away.

Last month, at the second session, President Bush indicated that the Administration was committed to further study, rather than immediate action.

Why does the Administration appear to be backing away from its initial recognition that we need to act rather than just continue studying?

Mr. SMITH. I don't believe the Administration is backing away. I think we need to do both. There are certain actions we need to take, and we definitely do need to continue studying and put forward a very substantial research budget, which I think is necessary.

What Secretary Baker said and repeated again in the speech to the Governors Association, which I have submitted for the record, is that we don't need to simply wait for the results of all the research.

There's a number of prudent steps that we should be taking anyway. We should proceed to phase out CFCs under the Montreal Protocol. We should look for ways——

Mr. OBEY. With respect to that, what are we doing to in fact provide the assistance to Third World countries that will be needed in order for them to effectively accomplish that?

Mr. SMITH. We met in Geneva in a preparatory group for the London meeting of the parties and addressed that question for about a week.

No final decisions have been reached, but we're discussing the possibility of supporting a clearinghouse mechanism, we're also talking about the possibility of a fund contributed on a voluntary basis by the parties, which might be administered through the World Bank.

There's a range of possibilities we're discussing to meet that need, and we'll be making final decisions on that in June in London at the meeting of the parties.

Mr. OBEY. What specific steps is State taking to ensure that negotiations on a global warming convention proceed as rapidly as possible and that they focus on setting strict goals for reductions in greenhouse emissions?

Mr. SMITH. Well, as I said, we've been supporting the IPCC process. The first step is to see the results of the interim report, which will address the science, the impacts, and the possible response strategies are, and it will include an indication of the issues that we'll need to include in a convention.

Our view is that the first step, as was the case with the Montreal Protocol and the Vienna Convention, is to do a frame work agreement and then consider specific protocols as they are needed on specific reductions.

Mr. OBEY. Well, back to that Montreal Protocol. What specific steps has State taken to date to identify the kind of special assistance which is going to be needed for those countries?

Has State calculated the magnitude of assistance which would be needed in order to achieve the goals of the Montreal Protocol?

Mr. SMITH. We have done a number of things in that regard, Mr. Chairman. Primarily under the leadership of EPA, there have been a number of country-specific studies of the needs that have been held, and, in fact, a number of other countries have bilaterally assisted in these studies in a number of developing countries.

We did have discussions in Geneva of what this was indicating to us, and the needs that we talked about in Geneva you can look at for the first three years with a great deal more confidence than you can for the next 20, as in most situations.

In that first few years, the numbers we discussed in Geneva were that in three years, looking at the needs we're starting to uncover, there might be an amount on the order of $100 million needed to respond to the needs of the current members of the Montreal Protocol, and that would increase if new developing countries join, and it might well increase after that three-year period as more CFC substitutes are developed and the need to get them produced and available to the developing countries increases.

GLOBAL CLIMATE CHANGE AND IPCC

Mr. OBEY. As you know, a frequent criticism from the environmental groups on the workings of the Intergovernmental Panel on Climate Change is that our efforts are recreating research that's already taken place.

Also, GAO has indicated that the Executive Branch has not established a coordinated National policy to guide Federal agency efforts relating to global climate change.

GAO also claims that no agency has yet been tasked with providing overall policy direction. What would your response be to that?

Mr. SMITH. Well, I have read the GAO report. I think it's mainly a problem of that having been written before we have done some things.

There has been established since that was written the so-called Bromley Group, led by Dr. Bromley, the Science Advisor, which meets regularly to provide exactly this high level policy guidance in this area, and we, I think, are doing quite well in terms of interagency coordination in policy on that, better than we were doing perhaps at the time the GAO report was researched.

Mr. OBEY. I have a few other questions on that subject for the record, which I'll submit to you.

[The information follows:]

SUBMITTED TO DEPARTMENT OF STATE

Question. When specifically do you anticipate that research on global climate change will yield conclusive results?

Answer. Because there are many aspects of the earth system which are not fully understood, it is not possible to predict when "conclusive results" will be available. However, it appears likely that the information needed to develop an adequate understanding of the factors which may lead to climate change will be obtained sometime over the course of the next decade through the U.S. Global Change Research Program and cooperative international research efforts. The Committee on Earth Sciences, which is coordinating the U.S. Global Change Research Program, states in its report that the program's goal of establishing the scientific basis for policy decisions related to global change can be met because:

"The sciences essential to an understanding of global phenomena have matured dramatically in the last few decades and are now positioned to address many of the questions that must be answered to truly understand and predict global change . . . many of the methodologies and research tools needed to address the global scales of change now exist, are proven, and can be fully exploited in the 1990's."

Question. What is the status of executive branch efforts to develop a coordinated national policy to guide federal agency efforts related to global climate change? When can we expect to see such a policy?

Answer. A Domestic Policy Council (DPC) Working Group on Global Change, chaired by the Assistant to the President for Science and Technology, was established last October with the charge of developing a coherent U.S. domestic policy on global change. To support the development of national policies on potential climate change, the Domestic Policy Council's Working Group on Climate Change has directed subgroups to review three key aspects of this issue. These are: (1) a review and synthesis of information on the economic impacts of climate change and policy responses, coordinated by the Council of Economic Advisors; (2) investigation into possible roles for the private sector, coordinated by the Departments of the Interior and Energy; and (3) an analysis of legal precedents for international agreements and conventions to address climate change, coordinated by the Departments of State and Justice.

Question. What is the status of the Intergovernmental Panel on Climate Change and what can we expect from the international panel?

Answer. The IPCC's three Working Groups on science, impacts, and response strategies are in the process of completing their reports to the IPCC. These reports will be finished and an overall IPCC report prepared during the course of the summer. The IPCC's first assessment report will then be adopted at the panel's fourth plenary session in Sundsvall, Sweden from August 28–31.

Question. The Administration requested $100,000 for the Intergovernmental Panel on Climate Change. This was the same level we funded the IPCC at in FY 90. What will this money be used for?

Answer. The U.S. $100,000 contribution to the IPCC is for administrative requirements of the IPCC Secretariat in Geneva. This includes Secretariat staff salaries, translation, publication and distribution of reports, support for IPCC meetings, etc.

Question. What progress is the IPCC making with respect to coordination with other U.S. agencies? When will Congress see results from the IPCC Working Groups? Please provide for the record a timetable for upcoming IPCC meetings and a schedule for reporting on all three Working Groups.

Answer. U.S. agencies are actively involved in all aspects of the IPCC's work. About 20 U.S. agencies and executive offices are involved in the various scientific, technical, and policy related aspects of the IPCC. U.S. participation in the IPCC in general and the Response Strategies Working Group (WGIII) in particular is coordinated through the Department of State. The Committee on Earth Sciences, through representatives from NASA and NOAA, coordinates U.S. participation in the IPCC Science Working Group (WGI), while the National Climate Program Office in NOAA coordinates U.S. participation in the Impacts Working Group (WGII).

The IPCC's three Working Groups on science, impacts, and response strategies are in the process of completing their reports to the IPCC. These reports will be finalized and the overall IPCC report prepared during the course of the summer. The IPCC's first assessment report will then be adopted at the panel's fourth plenary session in Sundsvall, Sweden from August 28–31, after which it will be available for public distribution. A schedule of IPCC meetings is attached.

UPCOMING IPCC MEETINGS

April 23-24.—IPCC Working Group III, Subgroup on Energy and Industry, Toronto.

April 23-25.—IPCC Working Group III, Subgroup on Resource Use Management, Geneva.

April 26-27.—IPCC Working Group III, Subgroup on Agriculture and Forestry, Geneva.

April 26-28.—Meeting of IPCC Working Group III topic corrdinators on economics and financial measures, Paris.

May 23-24.—IPCC Working Group III Energy and Industry Subgroup preparatory meeting on Noordwijk remands, Paris.

May 23-25.—Meeting of IPCC Working Group I to adopt report on science, London.

May 28-31.—IPCC Working Group II, approval of WGII report on impacts, Moscow.

June 5-8.—Meeting of IPCC Working Group III to adopt report on response strategies, Geneva.

June 11-14.—Meeting of IPCC Working Group III Energy and Industry Subgroup experts to consider Noordwijk remands, London.

June 18-20.—IPCC Report Drafting Committee, Geneva.

August 27-30.—IPCC Fourth Session, approval of first assessment report, Sundsvall.

October 29-November 7.—Second World Climate Conference Geneva.

PAKISTAN ENERGY PROGRAM

Mr. OBEY. Let's turn to energy planning. I'm trying to run through as many of these as possible before we have to go to the floor for the supplemental.

There's a significant degree of criticism with respect to your program in Pakistan—the energy program. Mr. Prickett, I think, specifically mentioned it. How would you respond to the criticisms of our efforts in Pakistan in terms of developing energy capacity which is based more on their renewable energy than fossil fuels?

Mr. EDELMAN. I can't respond, Mr. Chairman. I'm not familiar with the details of the Pakistan program. I'd be glad to get someone more knowledgable to chat with you or your staff about it, or submit some information for the record, whichever you'd like.

I know there is a major fossil fuel program going on there, but that's about the extent of what I can tell you.

Mr. OBEY. Let's get back together on that.

[The information follows:]

A.I.D. response. A.I.D. is playing a critical role in helping Pakistan meet its growing energy needs. The emphasis of the program is on least-cost energy planning and efficiency as well as promoting private investment in economically and environmentally sound energy resource and power development. The energy efficiency project is the most comprehensive in the developing world. A.I.D. is supporting the government's initiative to attract private investment in power. U.S. energy companies have submitted investment proposals for private power projects based on hydro, natural gas and coal. A.I.D. has made it clear that environmental concerns are extremely important and we are providing assistance to the Government of Pakistan to ensure the environmental soundness of these projects. The Government is committed to using fluidized bed and other clean energy technologies.

A U.S. private developer has been authorized to proceed with the development of a 10 Megawatt hydropower plant—one of the first private renewable power generation project of this size in the developing world. A.I.D. recognizes the importance of renewable energy and is working to move it into a more prominent position in Pakistan through a subproject that will collect data and draft "Requests for Proposals" for additional hydropower sites suitable for privately owned and operated power plants.

THAILAND BIOLOGICAL DIVERSITY PROGRAM

Mr. OBEY. Let me ask you, I read a number of interesting memos which have gone back and forth between various people at A.I.D. and also a number of State Department cables with respect to the biological diversity program in Thailand.

There has been significant criticism of A.I.D.'s backing away from that program. My question is why does the Asia/Near East Bureau appear to be messing up that program in Thailand?

Mr. EDELMAN. I have not stopped beating my wife, but I'm afraid I have to give you the same answer to that one as I did to the last one.

I'm not familiar with the details of that program either. In fact, I found out just before I came here that there was some controversy involved in the Thailand program.

Mr. OBEY. My concern, having read these cables, is that originally there was strong intent on the part of the people in the field to deal on a comprehensive basis with the environmental sustainability questions associated with the economic development program in that country.

One of the witnesses said this morning they think it's pretty crazy to continue to endorse an economic development program which is not environmentally sustainable in a country over the long haul.

Yet, if you review the cable traffic and if you review the internal memos in A.I.D., some of which we have received, apparently you had a decision made in Washington by the people in that bureau to set up a whole different series of hoops for those environmental considerations to jump through.

I frankly think we have some real problems with the way they are administering that program. Unless we can have some assurance that they are not going to have problems, I do not see what choice we have except to either try to limit money that is being spent in that country, period, or else engage in the kind of micromanaging that we were urged earlier not to do.

I would prefer not to do that, but I would ask you to go back to Ms. Adelman and find out why they are dragging their feet on this program.

I recognize the importance of the economic considerations involved, but somebody said a long time ago that if you took all the economists in the world and laid them end to end, that would be a good thing. Sometimes economists don't recognize that economics is not just numbers—it's cultural, it's societal, it's sociological, it's environmental. If you do not have all of the vibes right, you're going to get a pretty lousy song.

So it just seems to me that bureau is insufficiently aware of the Congress' determination to see to it that the economic development policy that is followed is sound from a resource base standpoint. I do not think we are getting that kind of response out of that group based on the stuff that we have read.

Mr. **EDELMAN**. Let me just say, Mr. Chairman, that what you say you're looking for, I am, too. I don't disagree with what you said about how everything has to go together, nor do I disagree with what you said about economists. I will look into that question, and we can get back with you or with the staff.

[The information follows:]

A.I.D. response. Biological diversity is an important component of the Bureau for Asia, Near East and Europe's (ANE) overall approach to the environment. The Bureau's draft Strategy for Environment and Natural Resources cites destruction of tropical forests and coastal ecosystems as one of the five key problems in the region. In Thailand, the conservation of biological diversity is an important concern which is of mutual interest to the U.S. It is a key component of the Management of Natural Resources (MANRES) Project. Conservation activities, being implemented by the U.S. National Park Service and World Wildlife Fund, were two of the first activities put in place last year. Future adjustments for the entire Thailand program are expected due to reductions in staff and funding levels and a review of the entire program is underway. However, we can assure you that the ANE Bureau views environmental concerns, including biological diversity, as an integral aspect of economic growth and that they will both remain important elements of the Agency's future program in Thailand.

MOROCCO HIGH ATLAS WATERSHED PROJECT

Mr. **OBEY**. Okay. Would you also give us a complete description of the Atlas Watershed Project so that we can understand again the rationale for backing away from the urgently suggested environmental program in Morocco?

Mr. **EDELMAN**. We'd be glad to.

[The information follows:]

A.I.D. response. The Project Identification Document (PID) for the Morocco High Atlas Watershed Project, which is the preliminary project design document, was sent to Washington for approval in November 1989. The review of the PID by the ANE Bureau resulted in agreement that water management issues in Morocco are of key importance to natural resources development with clear implications for the country's future economic growth. However, the ANE Bureau decided that further technical and policy issues constraining sound watershed mangement needed to be analyzed, using available FY 1990 funds, before further design of the project took place. In recent discussions with the Government of Morroco this year, we reached consensus on the need for a more comprehensive approach to addressing water policy and management issues. A.I.D. will be putting together a technical assistance team to work with Morocco's key water policy ministries which we hope will lead to a significant project in the near future.

A.I.D. ENVIRONMENTAL STAFFING

Mr. **OBEY**. We are running out of time. Is it true that A.I.D. has only one full time person staffing the early warning system to police what the banks are doing?

Mr. **EDELMAN**. I wouldn't be surprised if that is true, because most of the work on the early warning system is done in the field.

We rely on the field missions to talk to their World Bank counterparts and police these programs. They then send cables into Washington, in essence flagging the problems that they see. They know better out there what these programs are, and they certainly understand better what the problems may be with them than we can back in Washington.

The person back here is primarily a coordinator of gathering data together and then having a focal point back here.

Mr. OBEY. Is it true that the staff person responsible for coordinating and monitoring, as well as interpreting project information, has to monitor it, has to interpret the information, and has to provide their own clerical work?

Mr. EDELMAN. I don't know about the clerical work, but I don't think that the burden on the one person is as bad as it sounds. The analysis is done in the field. It isn't just that one person who goes and beats up on the World Bank or brings these potential problems to the attention of the World Bank.

It's more like the traffic cop—somebody who sees what's coming in and then farms it out. That does not do most of the analysis. It's the mission in the field that's responsible for doing that analysis, along with the appropriate people in the regional bureaus back in Washington.

Mr. OBEY. Are you planning to increase A.I.D. staffing for that purpose?

Mr. EDELMAN. We are looking now at the whole problem of A.I.D. environmental staffing. The flexibility that has been provided to us at the initiative of this committee, along with the Senate, in the appropriations bill for fiscal year 1990 will allow us to hire additional staff out of program funds.

We intend to do that, and we're now looking at the overall plan of where we need to put people and how many people can we afford. We don't want to use up all our program funds on people, but want to do some projects as well.

On the whole issue of staffing, we intend to dramatically increase both the staffing and the training of A.I.D. people, using that flexibility you've given us, and which I certainly hope you will continue to give us next year.

Mr. OBEY. I would like you to provide us for the record a detailed accounting of how A.I.D. intends to comply with Public Law 101-167 in terms of increasing the environmental staff at all levels; how many of those positions you expect to fill with environmental specialists, particularly the kind of specialist who would understand the complexities of biological diversity; and, how that will be translated in the Washington bureaus, especially the Asia/Near East Bureau, which I expressed concern about earlier.

Mr. EDELMAN. We are planning to hire technicians with those funds, not generalists.

[The information follows:]

A.I.D. response. For end use energy efficiency, renewable energy, and environmental activities, A.I.D. is taking steps to hire and support up to 20 employees (plus support staff) each year for three years. In January, overseas missions and regional and technical offices in Washington were queried regarding the feasibility of establishing program-funded environmental positions. A personnel hiring plan was prepared in March to determine how best to establish and fill positions for which there are program needs and available funds.

Bureaus and offices are moving ahead to specify, establish, and fill environmental positions with qualified individuals. To date, the status of FY 1990 positions is:

Global Warming Advisor (Mexico), being advertised;

Global Warming Advisor (Brazil), being advertised;
Global Warming Advisor (LAC Washington), to be advertised;
Environmental Project Manager (ANE Washington), to be advertised;
Natural Resources Economist (ANE Washington), to be advertised;
Environmental Program Manager for Eastern Europe (ANE/Washington), to be advertised;
Industrial Pollution Specialist (ANE/Washington), on board;
Environmental Specialist, Foreign Service National (Bangladesh), to be advertised;
Natural Resources & Energy Policy Advisor (AFR Washington), on board;
Global Climate Change Advisor (AFR Washington), to be advertised;
Environmental Training Specialist (S&T/Energy), on board;
Environmental Specialist (S&T/FENR), to be advertised;
Global Warming Advisor (S&T/FENR), to be advertised;
Pest Management Advisor (S&T/AGR), to be advertised;
Animal Agriculture Systems Advisor (S&T/AGR), to be advertised;
Senior Ecologist (S&T/AGR), to be advertised;
Regional Land Use and Environmental Planner (PRE/Housing Jamaica), being advertised;
Environmental Economist (PRE/Housing Washington), to be advertised;
Senior Ecologist (A&T/AGR Washington), to be advertised.

We expect that the list of positions will grow as project initiatives are developed at the country level during the next two fiscal years and are approved throughout A.I.D.

The S&T Bureau is bringing on board a very experienced biological diversity expert this summer. As the need for additional highly specialized expertise can be determined, we will make plans to fill such a need. At the present time, A.I.D. has programmed more than $30 million in FY 90 for support of biological diversity activities, a significant increase from earlier levels.

ZIMBABWE ELEPHANTS

Mr. **Obey**. The committee has been told recently that A.I.D.'s elephant project in Zimbabwe is not functioning as it ought to function.

One of the claims, for instance, is that Zimbabwe does not have an overpopulation of elephants, but rather it has lured them across the border from neighboring countries. The culling operations that result from that so-called overpopulation have resulted in the killing of 4,000 elephants per year. Meat sales from that culling did not benefit the poor villages to the extent intended. What do you know about that?

Mr. **Edelman**. The little bit that I do know about it is that according to the African Wildlife Foundation, Zimbabwe has about 68,000 elephants, about 24,000 of them that it considers surplus.

They do go back and forth across the border, we don't know how many——

Mr. **Obey**. But haven't they established a special system which, in fact, attracts more and more elephants into their territory?

Mr. **Edelman**. I don't know.

Mr. **Obey**. That's our understanding.

Mr. **Edelman**. I'll be glad to find that out, too.

[The information follows:]

A.I.D. response. Mr. Chairman, elephant conservation has been one of the emphases of A.I.D. biodiversity efforts in Africa over the past several years. During FY 1990 alone, A.I.D. plans to obligate over $12 million in direct support of programs that are a part of the African Elephant Conservation Plan, one of which is the Zimbabwe Department of Wildlife Research program that you mentioned.

Elephants migrate according to the season and the availability of food and water. While migration between Zimbabwe and Zambia is minimal due to the physical features of the border (Lake Kariba and the Zambeze River), the border between Zimbabwe and Botswana is a natural migratory route for elephants. Therefore, the elephant population of these two countries fluctuates, but is estimated at 45,000-50,000 each by the African Elephant Conservation Coordinating Group. Both governments believe that this is too large for the amount of land available.

The Government of Zimbabwe determines the carrying capacity of its wildlands and makes it wildlife management decisions on the basis of long-term monitoring of habitat resources and the wildlife population. As a result, certain wildlife species including elephants are culled, just as in certain areas of the United States white tail deer are culled to prevent overpopulation and degradation to the overall wildlife habitat. Under the monitoring and evaluation component of the A.I.D. project, we will investigate the methodology and impacts that the wildlife population research activities are having upon the sustainable management of wildlife.

The Zimbabwe wildlife program is specifically designed to provide benefits to the rural population well beyond just a source of protein. The primary goal is to provide economic benefits to the impacted populations in a way which will demonstrate the advantage of prudent wildlife management techniques and encourage them to become allies and partners in Zimbabwe's efforts to manage wildlife resources in an economically and environmentally sustainable manner.

WORLD BANK ENVIRONMENTAL FUND

Mr. OBEY. Okay. Let me ask a question with respect to the banks. As I understand it, the bank has proposed a new concessional lending operation which would fund projects concerning global warming, ozone depletion, and similar issues?

Is that in the works? What is the status of that, and what is the Treasury's position on it?

Mr. VUKMANIC. This proposal was an outgrowth of a proposal by the French Governor at the last annual meeting of the Bank and the Fund, in which the Bank was asked to develop a paper on the possibility of constructing a fund in the Bank for concessional lending on environmental projects.

That paper was discussed in Paris a week ago, two weeks ago actually, by all the members of the Bank. There were preliminary discussions held at that point and discussions will be held again around the Development Committee.

My suspicion is the fund will be created. The Treasury's position on it at this point is basically not to take a position.

We participated in the preliminary discussion and indicated that we had some concerns with regard to how this fund would operate, in particular with respect to the current operations of the Bank.

We, along with other governments, raised some questions along those lines and hope to have them addressed at the Development Committee.

One of the issues we are concerned about, obviously, is we don't see where we're going to have funding for this kind of an activity within the Bank given our current budget for the MDBs, so that is of concern to us.

But our major concern is how this fund would operate within the Bank's current operations.

Mr. OBEY. If that fund or anything like it were established, how would your staff seek to establish demonstrable evidence that the Bank is, in fact, going to be making progress in the areas of forestry, biodiversity, energy efficiency, public access to information, and, for that matter, public participation in the discussion of the establishment of the fund?

As you know, there is a lot of criticism that the Bank is extremely elitist in terms of the way it approaches this problem.

I get the impression, frankly, that the Bank thinks that this whole environmental issue is a pain in the you know what. They will doff their hat to it to the extent that it's politically necessary, but they don't like it getting in the way of their continuing business as usual. Is that an unfair characterization of their position?

Mr. VUKMANIC. I don't think it's a totally unfair characterization of their position. I think one of the participants in an earlier panel indicated that this issue is not a short term issue, that it's a long term issue.

I think we have to take that approach with regard to the Bank, all of the banks, on this issue. I think the Bank is coming around.

I think they're coming around a lot more quickly than they were in the past, so I don't think they're at a point of just doffing their hat.

I think they realize that this issue is not going to go away, and they have to address it realistically. With regard to how we would endeavor to find out whether, in fact, the Bank is doing all of the things you've said in the environmental area, collaboration, et cetera, I think we continue to look at the Bank's operations with regard to specific projects and to monitor them very closely.

Our ED's office is extremely active in this area, not only in monitoring, but in trying to influence. We continue to have conversations with NGOs and invite those conversations to get their viewpoint and their information with regard to projects, et cetera.

Mr. OBEY. I will submit several other questions on this to you for the record.

[The information follows:]

SUBMITTED TO DEPARTMENT OF THE TREASURY

Question. In the World Bank's February 1990 discussion paper entitled "Funding for the Global Environment," a proposal is discussed for a new environment facility within a Bank. Within this paper, the Bank cites its efforts to improve environmental policies and programs in borrowing countries, but notes that additional efforts may be needed to combat problems which are global in nature. It also details how the Bank, UNEP and UNDP might work together through a separate environmental facility such as that proposed by France during the September 1989 Development Committee meeting.

Support for a major environmental funding facility is reported from several other donors, including France and Germany, who have indicated willingness to make major contributions to it. Discussions were held in March in Paris with a number of donor agencies. What is the United States position on establishment of this facility?

Answer. The United States strongly supports efforts to address global environmental issues in the World Bank and the regional development banks. We have taken the lead in promoting MDB programs affording greater protection of tropical forests, more reliance on energy efficiency and conservation, preparation of environmental impact assessments and preparation of environmental action plans for borrowing countries.

We do not, however, at this time, support the proposal to establish a separate facility or "green-fund" within the World Bank. We have encouraged the Bank to utilize its existing resources to establish action plans or programs that can address the issues that have been identified in the proposal.

Question. How would such an environment facility relate to the environment department at the World Bank and other MDBs?

Answer. This is an issue that we have emphasized in our discussions with the World Bank and other potential donors to the facility. We have been particularly concerned that any such effort should not detract from on-going environmental work that we believe is very important such as energy efficiency and conservation, protection of tropical forests, environmental impact assessment and environmental action plans. The World Bank has already made commitments to achieve greater progress in all of these areas as a result of the IDA 9 Replenishment Agreement. Accordingly, we have raised questions about the additional environmental benefits that could be expected as a result of the establishment of the facility and whether or not the Bank would enhance its ability to deal effectively with environmental issues. We have also questioned whether or not the Bank has the appropriate policies and practices in place and is appropriately staffed to take the additional environmental initiatives that might be necessary.

Question. What is the current level of funding under discussion to establish this new environment facility? Would grants as well as loans be part of its operations?

Answer. The current proposal envisages funding of $1.0 billion over a period of three years. It has also been proposed that the funds should be made available either as grants or on a concessional-basis.

Question. What countries are involved in pursuing the establishment of a separate environment facility? To date, what countries have volunteered to fund the facility, and at what level?

Answer. A number of countries participated in the meeting that took place in Paris in March of this year. Those countries included: Australia, Austria, Belguim, Canada, Denmark, Finland, France, the Federal Republic of Germany, Italy, Japan, the Netherlands, Norway, Spain, Sweden, Switzerland, the United Kingdom, and the United States. Thus far, only France has said that it is interested in principle in contributing a specific amount of money to the facility (i.e., 900 million French Francs).

Question. While I support the Bank's goal of devoting more resources to environmental problems, I'd like you to convince me that Treasury is taking adequate steps to ensure that the Bank demonstrates its ability to manage such additional funds through substantial improvements in its existing programs and policies.

How will your staff actively seek demonstrable evidence of Bank progress in the areas of forestry, energy efficiency, environmental impact assessments and public access to information?

Answer. We have always taken the position, in meetings of the Development Committee, in the IDA 9 replenishment negotiations, and in bilateral discussions with Bank staff and management and other members of the Board, that the World Bank should make substantial improvements in its on-going environmental activities and as part of its existing lending programs and policies.

We have devoted a great deal of effort to the review of tropical forestry projects that have come to the Board of the Bank over the past year. We have urged the strengthening and reform of the Tropical Forestry Action Plan (TFAP) so as to place greater emphasis on forestry conservation and protection of biological diversity and to make the TFAP, itself, a more open process. We have also urged the Bank to play a more active role in facilitating debt-for-nature swaps and to use these swaps more innovatively to help address environmental issues.

Energy efficiency and conservation have been given similarly high priority in our dealings with the Bank. This was an important theme in negotiations for the replenishment of IDA, during which we urged reforms in the Energy Sector Management Assistance Program (ESMAP) and greater promotion of renewables and integrated least-cost planning in borrowing countries. The World Bank is now undertaking a high-level review of ESMAP and is cooperating with the U.S. Department of Energy on a program to promote the use of renewables in several countries in Asia.

As you know, it was very largely at our urging that the World Bank adopted environmental impact assessment procedures in September of 1989, and we have been monitoring the implementation of these procedures very closely over the past several months. The Bank has provided training to members of its own staff on environmental impact assessment and sponsored additional training programs in this area in a number of its member countries. It has also undertaken modifications in the monthly operational summaries to provide additional environmental information on upcoming projects and to assign each of those projects a classification based on its expected environmental impact.

Question. My feeling is if we're going to do this, and I frankly think we would be moving in the right direction if we do, we have got to do it right from the very beginning of this process. Again, convince me that this Committee's concerns will be met in any proposal Treasury supports regarding this lending facility.

Answer. We have taken very much this same approach in the first meeting of potential donors to a green-fund within the World Bank that was held in Paris in March of this year and in a meeting of the Development Committee of the World Bank that was held in Washington in May. At the meeting of the Development Committee, we said that we were not in a position to support the establishment of a separate facility or green-fund within the World Bank and that we encouraged the

Bank to utilize its existing resources to establish action plans or programs that could address some of these issues. At that time, we believed that more work needed to be done on the potential funding and operation of a green-fund.

Question. Finally, will Treasury demand that the Bank actively solicit public participation in discussions of the fund?

Answer. At the meeting of potential donors that took place in Paris in March, the United States specifically urged the World Bank to consult with the academic and scientific communities and with non-governmental organizations about the proposal. It is our understanding that the process of consultation has already begun.

WORLD BANK PROJECTS WITH ADVERSE ENVIRONMENTAL IMPACTS

Mr. OBEY. Let me ask you, with respect to specific projects, what about the Narmada Valley development in India? I think there has been many objections raised to that project. How do you evaluate the Bank on that project. What is the U.S. doing on it?

Mr. VUKMANIC. I think if I were to evaluate the Bank, I would have to know what they've done most recently, and I don't, but let me give you a little history.

I think if the Bank had to do the project today, the Bank, by their own admission, would not do it. The Bank started this project, something in the order of 10 years ago, if I'm not mistaken. The Bank has tried, through a variety of techniques, to get some progress on some of the resettlement issues and some of the environmental issues.

I think one of the problems the Bank has in this particular project is they believe that their presence will be more helpful than hurtful in the long run.

Now, there is a massive difference of opinion as to whether that is a correct assessment or not, and a lot of people would like to see the Bank just back out 100 percent.

Mr. OBEY. How much more money is expected to be put into that project?

Mr. VUKMANIC. I can't give you that number specifically, but I'll be happy to provide it, but it is a fair amount. I don't think more than 50 percent of funding has been provided at this point. That's my estimate.

Mr. OBEY. How many projects are there for which the Bank is providing funding for now that the Bank would not have proceeded with if they had the decision to make again?

Mr. VUKMANIC. That I really can't answer at this point, but I will stick my neck out and say I don't think there are all that many.

There are a few, certainly, and those few stick out like sore thumbs.

Mr. OBEY. Which are the few that you're referring to?

Mr. VUKMANIC. There have been dam projects, in particular, in Latin America and India where the Bank has become involved and has run into problems not only of resettlement, but siltation and other problems, which have, in some instances, led the dams to be inefficient and inoperative. So there are a few.

MDB ENVIRONMENTAL IMPACT ASSESSMENTS

Mr. OBEY. The World Bank states that environmental assessments are already standard procedure for most projects. Do directors generally receive the environmental assessments prepared under the World Bank EA directive?

Mr. VUKMANIC. Let me clarify one thing. The assessments that are currently being done, sort of environmental information or the impact on the environment, is being done by many of the banks, not just the World Bank, but they are not an environmental impact assessment as defined under the IDA agreement and as we've pursued elsewhere.

Those assessments have yet to be put into place and the procedures for them finalized. A directive was issued by the bank, but we haven't seen them.

The Executive Directors, once that process is in place, and we hope it's in place shortly, will receive the environmental impact assessment, that's correct, and they should receive it 180 days in advance of Board consideration.

Mr. OBEY. When will you be able to tell us that the Directors have adequate access to environmental information concerning proposals that they are called to vote upon?

Mr. VUKMANIC. I think they're getting good access now. I don't think they're getting the kind of access in terms of the quality of work that we would like to see, and I think the Bank agrees and has decided to move in the direction we want.

Hopefully, it will happen soon, but I can't give you a definitive date.

Mr. OBEY. Can you tell me how often over the past two years the directors requested additional information on environmental impact of a specific project?

Mr. VUKMANIC. There have been cases, but I can't give you the exact number. I'll be happy to provide it, but there have been cases.

Mr. OBEY. Can you show us how many times U.S. officials have requested additional information?

Mr. VUKMANIC. Certainly. One you've raised already is Narmada, and another that comes to mind is the Brazilian Electric Power II. There have been other forestry loans in which we've intervened, one in Sri Lanka that I'm familiar with.

Mr. OBEY. Okay. I'm just out of time. I have a number of other related questions I am going to ask you to provide for the record.

[The information follows:]

SUBMITTED TO DEPARTMENT OF THE TREASURY

Question. The World Bank states that environmental assessments are already standard procedure for most projects. Do the Directors generally receive the environmental assessments prepared under the World Bank EA Directive? [If not, do they receive information derived from these assessments?]

Answer. The World Bank adopted an operational directive on environmental impact assessment in September, 1989, and is now in the process of implementing that operational directive. The implementation process will take some time. All new projects now entering the pipeline are covered by the provisions of the directive and receive an environmental classification that is published in the monthly operational summary. However, thus far, no projects have come to the Board for which environmental impact assessments have been completed under the provisions of the directive. This does not mean that environmental impact assessments have not been prepared for any of the projects that have been funded by the Bank or currently under consideration. However, as a matter of policy and practice these assessments have not previously been made available to the Board of Executive Directors. Executive

Directors have received environmental impact assessment information only as part of the information that is contained in the project appraisal report-and in the form of additional material received in response to specific requests they have made.

Question. What are current policy guidelines for U.S. Executive Directors to assure that environmental impacts have been taken into account; are they directed to try to obtain EA information for projects on which they are voting?

Answer. Executive Directors have been directed to seek the adoption of procedures within the MDBs that would result in environmental impact assessments for projects that will have a significant effect on the environment. The Executive Directors have also been directed to assure that the assessments are made available to the Board at least 120 days in advance of Board action. They have also been instructed to seek additional information on the environmental aspects of specific projects that will assist them in their consideration of the projects.

Question. Do the Directors have access to adequate environmental information concerning impacts of proposals on which they are voting?

Answer. Executive Directors have not had access on a systematic basis to environmental impact assessment information. The environmental conditionality of the IDA 9 Replenishment Agreement was designed expressly to correct this situation. Some environmental impact assessment information is contained in the project appraisal reports and Executive Directors seek additional information on this aspect of specific projects as they believe it is needed to assist them in the voting decision.

Question. Are you satisfied that assessments are done on all the projects that need them—that have significant environmental impacts?

Answer. Environmental impact assessments are clearly being completed for many of the projects funded by the MDBs. This has been done as a matter of national law in some of the borrowing countries and at the Bank's initiative in other borrowing countries. However, we have not had systematic access to the information that would be required to fully assure ourselves on this point. My own view is that there are a number of projects that have not had adequate environmental impact assessments and that the procedures we are seeking to establish will be helpful in correcting this situation.

Question. How often over the past year have the directors requested additional information on environmental impacts or effects of proposals before them? Are responses to such requests satisfactory in providing needed information?

Answer. I would estimate that we have asked for such additional information on about thrity projects over the past year. In some of those cases, the information had not been clearly presented in the appraisal report or it had not been clearly presented in the appraisal report or it had not been included in the appraisal report, even though it was available to Bank staff. In other cases, we sought information about specific projects in advance of board consideration and it has been included in the appraisal report. The responses to our requests have generally been satisfactory.

Question. Do you consider the environmental assessment procedures issued by the World Bank adequate? Will they meet the requirements of the environmental assessment section of P.L. 101-240, described above?

Answer. The environmental impact assessment procedures adopted by the World Bank in September 1989 represent a significant step forward and should be adequate if they are implemented effectively. We will be monitoring this implementation process very closely. The IDA 9 Replenishment Agreement clearly specifies that Executive Directors will receive copies of environmental impact assessments of IDA projects at least 180 days in advance of Board consideration. There is no parallel provision that was negotiated as part of the World Bank's General Capital Increase several years ago, but we have urged the Bank to follow the IDA procedure for IBRD loans as well as for IDA credits. We hope they will do so.

Question. Do your anticipate problems obtaining information on environmental impacts 120 days in advance of a vote on a World Bank or other MDB proposal?

Answer. The World Bank and the Inter-American Development Bank should be able to meet this requirement by the end of 1991. Both of these banks have already adopted environmental impact assessment procedures and begun the training of their own staffs and the staffs of agencies in borrowing countries. There may be some problems with the Asian Development Bank which clearly needs to build up its environmental staff and make a number of changes in the procedures it has already adopted for assessing the environmental impact of projects in order to meet this specific requirement. I am also concerned about the African Development Bank because it is very seriously under-staffed in the environmental area and has had a number of problems in developing procedures for the appraisal of projects.

Question. What measures will the Treasury Department take to assure that the requirements of this law are met?

Answer. We have advised all of the MDBs of this particular requirement. We will make strong environmental conditionality, including specific provision for this particular requirement, an important element of upcoming negotiations for replenishments of these institutions. If the requirements of this law are not met, we would plan to begin abstaining on or voting against loans that would have a significant effect on the environment.

Question. Please describe the organization within the Treasury Department for reviewing environmental impacts of MDB proposals?

Answer. Currently, two staff members within the Office of Multilateral Development Banks are responsible for all the environmental aspects of U.S. participation in the World Bank and the regional development banks. One of the most important elements of their overall responsibilities is the review of the environmental impacts of specific projects. They work closely with personnel from the Department of State, the Agency for International Development, the Environmental Protection Agency, and other departments and agencies in identifying environmentally problematic aspects of upcoming loans and in seeking to effect changes that will mitigate or eliminate adverse environmental impacts.

Question. How many staff are involved in such review? Are such staffing levels adequate?

Answer. The environmental workload has become particularly heavy over the past several years. In addition to the review of the environmental impacts of individual loans, this workload has involved oversight of the general process of environmental reform in the MDBs, the environmental elements of replenishment negotiations, discussions about the proposal for establishment of a green-fund within the World Bank, environmental elements relating to the establishment of the European Bank for Reconstruction and Development, the preparation of congressional testimony on environmental topics in the MDBs, and detailed and extensive reporting to Congress on a very broad range of environmental initiatives now under way in the multilateral development banks and in other international organizations.

We have submitted a request for additional budgetary support in the environmental area, including provision for two additional staff members and increased funding for Treasury participation in international environmental meetings related to the MDBs and closer oversight of the environmental work now going on in the individual banks. This additional budgetary support will not become available until FY 1992. In the meantime, we have asked EPA and AID to consider the inter-agency transfer of two professionals to assist us in the environmental area.

Question. Are they currently hindered by lack of access to environmental information on projects or programs?

Answer. I do not believe that we are hindered by a lack of environmental information per se but I want to emphasize that it is sometimes very difficult and time-consuming for us to develop the specific environmental information that we need through meetings with bank staff and coordination with non-governmental organizations, other U.S. Government agencies and the agencies of other governments. This has been very much the case in our review of tropical forestry projects, for example.

Question. What efforts are made before a proposal is presented to Directors for a vote—in project preparation phases—to obtain information about environmental impacts, and to assure that such impacts are being taken into account?

Answer. We have made major efforts through the early-warning system to obtain environmental impact information and to see that it is taken into account in the appraisal of specific projects. The tropical forestry projects that we are examining again are a very good example of these efforts.

Question. Critics of the Narmada Valley projects in India being funded by the World Bank argue that environmental assessments were not done in a timely manner, and that environmental impacts have been ignored. How does the U.S. Executive Director assure himself before voting on projects that such problems have been addressed or resolved? How is this being done in the case of the Sardar Sarovar Dam in the Narmada Valley?

Answer. The Sardar Sarovar Project was approved by the World Bank in 1985. An environmental impact assessment was completed before the approval of the project. I do not believe that we raised problems about the completion of an environmental impact assessment at that time. Our problems have had more to do with the implementation of the project and the failure of the authorities in India to proceed with the studies that they were obligated to undertake as a result of the environmental impact assessment. As a general matter, we do the best that we can on the basis of the information that we have or are able to develop in cooperation with non-governmental organizations and other government agencies and the staff time that we are able to devote to the review of individual loans.

Question. How would you characterize the environmental performance of the various MDBs? Are environmental assessments being carried out in the regional MDBs?

Answer. Overall, all of the MDBs are making progress in various areas of environmental reform. Specific examples are the environmental impact assessment procedures in the World Bank and the Inter-American Development Bank, the new environmental line unit in the Inter-American Development Bank, the environmental policy paper in the African Development Bank, and the Asian Development Bank's continuing efforts to involve non-governmental organizations and local community groups in identification and appraisal of projects. However, this progress has not been uniform in all of the MDBs and there is a great deal more that needs to be done. The Asian Development Bank and the African Development Bank are both very seriously under-staffed in the environmental area and we have urged them to take steps to correct this situation. The Asian Development Bank needs to make specific changes in its procedures for environmental impact assessment and the African Development Bank has barely begun the process that should lead to the development of such procedures. The World Bank and the Inter-American Development Bank both must make major efforts to implement the environmental assessment procedures that they have adopted. The details of these reforms and the initiatives that Treasury has taken are contained in an annual report that was recently submitted to the Congress.

Question. To what extent are the regional banks prepared to deal with the environmental assessment requirements outlined for U.S. Directors in P.L. 101-240?

Answer. The World Bank and the Inter-American Development Bank should be able to meet the requirements for environmental impact assessment procedures by the end of 1991. There may be some problems with the Asian Development Bank which will have to make some changes in the environmental assessment procedures it has already adopted and significantly increase the number of environmental staff. I am more concerned about the African Development Bank which is also very seriously under-staffed in the environmental area and which has had a number of problems in developing effective procedures for the appraisal of projects that they wish to finance.

TROPICAL FORESTRY ACTION PLAN

Mr. OBEY. Can you simply tell me why so little of the TFAP funding is going into conservation of tropical forest ecosystems? Can anybody answer that?

Mr. VUKMANIC. I'm not sure of the answer, but as I indicated in our testimony, this is an area we have been trying to turn around. This is an area we're concerned about.

I think one of the criticisms that you raised in a previous testimony that I had given a year ago is that the bank did a lot of forestry loans, but they turned out to be management and little else.

One of the issues we'd like to see more on is preservation.

Mr. OBEY. I have a number of other questions with respect to TFAP that I am going to ask answers be provided for the record.

[The information follows:]

SUBMITTED TO DEPARTMENT OF THE TREASURY

Question. The September 1989 report by the Food and Agriculture Organization (FAO) on the TFAP Review Meeting validates some of these concerns. In 1988, 69 percent of development bank funding for TFAP went into forest-based industrial development, much of which involves support for infrastructure and industrial access to previously inaccessible forest area. When these investments are added to those of donor countries and U.N. organizations, of the total, $302 million or 32 percent of total TFAP funding is being invested in forest-based industrial development, $213 million or 22 percent is invested in forestry in land use (often reforestation or use of trees in agriculture-agroforestry); $158 million or 16 percent is invested in fuelwood and energy (often in plantations of trees for fuelwood); $188.7 million or 20 percent is invested in institution-building, usually forestry institutions, and just $83.5 million or under 9 percent is investment in conservation of tropical forest ecosystems.

Among donor countries, the United States is reported by FAO to have contributed $16 million to conservation of tropical forest ecosystems out of its total of $82.7 million for TFAP. This was far in excess of the other donors' contributions to this category of activity. Only 5 other countries contributed over $4 million. Only Canada and the U.S. contributed over $5 million.

There is wide agreement on the success of TFAP in focusing countries' attention on forestry and providing for coördination among donors in a forestry planning process. The TFAP process provides for the preparation of National Forestry Action Plans for each participating country (67 countries are now involved in the process) and in the final stages (only 3 countries are at this stage), specific projects are proposed for donor funding. However, the emphasis on forestry planning, often by forestry professionals, is felt by some to have the inevitable result of emphasizing timber extraction and plantation development, often to the exclusion of the TFAP's other expressed goals.

Why is so little of the TFAP funding going into conservation of tropical forest ecosystems, since protection of tropical forests is one of the major goals sought by most backers of the plan?

Answer. There are a number of reasons for relatively little funding going into conservation activities per se. These include country priorities, donor priorities, low capital intensity of conservation activities, low absorptive capacity in forested countries and conservation activities outside of the TFAP framework. Many countries with forests believe they cannot afford to finance conservation activities per se, especially if the loans are available only at near-market terms. Thus they are reluctant to give high priority to conservation activities either in the domestic budget or in the foreign assistance program. Donors may be looking for projects with high rates of economic return and conservation projects do not fit well into their priorities. However, it should be noted that some donors take a broader view of conservation. An industrial timber project which aims for sustained production is viewed as a type of conservation activity since the area is expected to remain under forest cover. The low capital intensity requirements of conservation activities sometimes give a distorted view of the level funding for conservation. Enormous amounts of money are not necessary while political will and institutional capacity are important accompaniments to the funding. Low institutional capacity in many developing countries, especially within those agencies responsible for environment, also deter or delay the flow of funding into conservation activities. Lastly, funding outside of the TFAP framework may be providing for conservation activities which would diminish the need for TFAP funding per se. Examples include projects by the World Bank, World Wildlife Fund and Conservation International.

Question. There is evidence that with additional research and market development, non-timber products from tropical forests can be economically developed. Is any of the funding for forestry based industrial development going into non-timber industries? How much?

Answer. Funding for forestry based industrial development generally refers to funding for timber extraction and/or plantations. However, the TFAP framework does include non-timber products. The investment figures are subsumed under the headings of agroforestry and fuelwood. Non-timber products include, among other things, rattan, fibers, medicinal plants, fruits and nuts, dyes, and fuelwood.

Question. Is the World Bank carrying out analysis of the direct impacts on deforestation the actions outlined in the existing national Forestry Action Plans would have?

Answer. Where the World Bank is involved in preparing a forestry or resource management project, the impacts of existing plans are analyzed. In a number of cases, the Bank has indicated to the governments concerned that planned timber harvest rates are unrealistic or unsustainable. In several cases, the Bank has delayed preparation for projects because of concern over environmentally unsound objectives on the part of the countries.

Question. Should the United States or the MDBs continue to support the Tropical Forestry Action Plan process if it does contribute to deforestation and the loss of biological diveristy? What steps can the United States take to assure that its actions are not contributing to such a result?

Answer. It is not clear that the TFAP process contributes to deforestation. What *is* clear is that the process has not lived up to expectations that it would halt or dramatically slow the rate of deforestation. The United States has been a vocal critic of TFAP projects which are judged to be incompatible with the goals of sustained timber production and preservation of biodiversity. The U.S. Executive Directors have voted against forestry and other projects in the MDBs which might have had detrimental effects on tropical forests. More importantly, the United States has cooperated with NGOs to shape projects so as to improve the possibilities for slowing or halting deforestation. Projects in Ivory Coast and Ecuador are examples.

Recently three reviews of the TFAP were issued. They were prepared by the World Rainforest Movement (a consortium of NGOs), the World Resources Institute (a U.S.-based NGO which helped originate the TFAP), and an independent panel appointed by the Food and Agriculture Organization (FAO) an originator of and the primary coordinator for the TFAP. All three reviews were highly critical of the TFAP process and the results thus far. The Department of Treasury has examined the reviews and concurs with many of the recommendations for improvement of the process. Treasury and the Agency for International Development will be working in the coming months to have the recommendations put into place. The MDBs are expected to review their TFAP activities in light of the analyses and recommendations. The U.S. Executive Directors will be pressing for such review.

Question. Do you agree that NGO participation has been lacking in the TFAP process? Would increased grassroots and NGO participation make a critical difference in the focus of TFAP on industrial forestry development?

Answer. NGOs and affected local communities have been largely left out of the TFAP process. There is no question that their involvement would have influenced the shape of TFAP programs and, very likely, improved chances for the success of projects. The United States has long pressed for increased consultation of and involvement by NGOs and community groups in all MDB projects. All three of the reviews mentioned above strongly advocate opening up the process and making information widely available. The U.S. strongly concurs with this view and will press for its implementation.

Mr. OBEY. Well, I have some more questions for you, but I will have to put them all in the record. I'm supposed to be over on the floor in five minutes.

Thank you all for coming. I'm sorry we put you on later than we thought.

[Questions and answers for the record follow:]

Questions for the Record From Mr. Obey

SUBMITTED TO DEPARTMENT OF STATE

ADMINISTRATION'S COMMITMENT TO ENVIRONMENTAL PROGRAMS

Question. What role should State and A.I.D. play in overseeing an environmentally focused foreign aid fund?

Answer. The Department of State and A.I.D. consult frequently on U.S. foreign assistance programs. A.I.D. has a wide range of projects addressing environmental issues, including but not limited for forestry, biodiversity, watershed management, urban and industrial pollution, coastal zone management, and land use planning. We expect to continue our close consultations as A.I.D. expands its involvement in environmentally related programs. .

Question. How does President Bush's commitment to help developing nations in developing environmentally sound plans translate into a cut in Administration requests for UNEP ($12 million to $10 million) and CITES ($750,000 to $500,000)?

Answer. The Administration FY 1991 request of $10 million for UNEP is in fact an increase of $2 million over our FY 1990 request of $8 million. Likewise, the FY 1991 request for CITES is 150 percent higher than the Administration's FY 1990 request. The United States is still the largest contributor to both organizations, reflecting its full support.

[CLERK'S NOTE.—The Department of State did not respond to one question regarding EPA's role in international environmental issues.]

UNITED NATIONS ENVIRONMENT PROGRAM

Question. What actions have been taken by the State Department to develop an action plan which defines U.S. objectives and priorities for U.S. participation in the environment program, including a specific plan for achieving them?

Answer. The Department of State, along with eighteen other government agencies, has identified benefits derived from UNEP activities, and participates in varying degrees in all of UNEP's programs. Throughout the year, the achievement of U.S. objectives and interest is evaluated as we constantly monitor UNEP activities. The UNEP Governing Council sessions are held biennually, and special sessions have been called recently in the alternate years, in 1988 and 1990. The Department of State manages an interagency process to review U.S. goals and objectives in preparation for these meetings, and then attends, participates in, and evaluates the decisions of these meetings in terms of U.S. interests.

—We are currently beginning our preparations for the 1992 U.N. Conference on the Environment and Development which will provide the principal forum for decisions on the role of the United Nations system in international environmental efforts for the remainder of this and the beginning of the next century. The Department of State is actively involved in seeking recommendations from all concerned executive branch departments and agencies for the U.S. delegation's participation in this summer's Preparatory Committee for the 1992 Conference. This process will occupy us for the next two years, providing among other things an opportunity for an ongoing evaluation of U.S. involvement with the U.N. Environment Program.

OZONE DEPLETING CHEMICALS

Question. The world's industrialized nations have committed to a phase-out of ozone depleting chemicals under the Montreal Protocol. Most developing countries, however, have so far refused to participate, including such relatively major CFC producers as India, China and Brazil.

Although the Third World now accounts for a relatively small share of global CFC use, future growth in CFC use in these countries threatens to undercut the goal of the Montreal Protocol.

Many developing countries recognize the urgency of eliminating ozone depleting chemicals. However, they remain hesitant to join the Montreal Protocol because they fear that phasing out CFCs and other ozone depleting chemicals will be prohibitively costly.

The parties to the Montreal Protocol have called for the establishment of a mechanism for financial assistance and technology transfer to these countries. However, I'm concerned that no specific measures have been proposed, either as to the mechanism or to the amount of aid required.

What steps has the State Department taken in identifying and proposing a mechanism for special assistance to these developing countries?

Answer. The State Department in consultation with other concerned agencies, is currently developing its position on a mechanism for special assistance to the developing countries, to facilitate their shift to substitutes for ozone depleting products, in preparation for discussions and decisions to be taken at the Second Meeting of Parties to the Montreal Protocol to be held in June, 1990.

From February 26-March 5, 1990, a meeting of a working group of Montreal Protocol participating countries, at which key non-participating countries, e.g. India and China, also attended, was held in Geneva devoted to the issue of assistance to developing countries ("Article 5 countries"). Three needs were considered: a) a coordinating committee of the parties to oversee the provision of assistance to Article 5 countries, b) a clearinghouse to facilitate national assessments of needs, to assist in the transfer of relevant technologies, and to maintain an inventory of proposed projects, and c) a fund to finance agreed incremental costs of acquiring substitute technologies and products in connection with the shift away from CFCs. EPA has agreed to contribute to the costs of establishing a clearinghouse facility under UNEP or other suitable auspices. The World Bank has indicated its willingness to consider working with the Parties as the manager of such a Fund element. At a May 9-11 working group meeting, the U.S. expressed support for the elements of an assistance approach which had been discussed, but indicated that in our view the World Bank did not need additional funds to carry out its role in this regard.

Question. Has State calculated the magnitude of foreign aid which will be required to achieve the goals of the Montreal Protocol?

Answer. Our very preliminary cost estimate for a funding mechanism to cover incremental costs for the initial three year period of operation of a funding mechanism under the Protocol indicates that total capital costs could be around 100 million dollars for the current Article 5 countries. UNEP officials estimate that an additional 100 to 200 million dollars might be needed if China, India and others joined at the beginning of that period. They also estimate a need for 18 to 20 million dollars during those years for the clearing house, technical assistance and coordination functions. Reliable estimates beyond that period are difficult to make, although requirements may well be higher as new technologies come on stream and the need arises to introduce them into LDC's.

AID TO ENVIRONMENTAL NON-GOVERNMENTAL ORGANIZATIONS

Question. Being an environmentalist is a deadly business in some countries. Chico Mendes, a leader of Brazilian rubber tappers, was assassinated last year, and a Zimbabwean army officer, Capitain Edwin Nleya, was killed in 1989, under mysterious circumstances after investigating a possible poaching conspiracy in that country's army. Has the State Department pressed for information on these cases, and expressed the concern of the U.S. government? Can the State Department point to any successes in protecting such individuals or organizations? How is the advocacy of a healthy environment or the preservation of biological diversity treated in the State Department's annual human rights report? In what countries is the advocacy of sewage treatment, the protection of endangered species, and similar activities, carried out at the risk of one's freedom—or one's life?

Answer. The Department of State takes an active interest in the rights of individuals to exercise freedom of speech and to engage in legitimate political activity. The U.S. expressed its concern to the Government of Brazil about the murder of Chico Mendes. Our Embassy in Brasilia has followed the investigation of the murder closely, as it will the trial, scheduled for June, of the two men accused of the murder. The Department has reviewed the Nleya case, but has seen no clear evidence that his death was related to his anti-poaching activities.

Our annual human rights report to Congress addresses areas, including environmental activism where appropriate, where these rights are restricted. As a rule, restriction of environmental activism tends to be tied to other factors such as ethnicity, economics or political persuasion. The Department of State has regularly, and with some success, intervened on behalf of individuals and organizations whose rights have been threatened on religious, ethnic, political or similar grounds. For example, at the November 1989 CSCE meeting in Bulgaria, the U.S. fought for recognition of the right of individuals, groups and organizations concerned with environmental issues to express freely their views, to associate with others, to peacefully assemble, as well as to obtain, publish and distribute information on these issues.

Question. How can the U.S. best assist such NGOs in improving environmental awareness in LDCs? Can these groups be trained to assist in environmental monitoring in their countries, e.g., in the control of poaching, illegal logging, water pollution, etc.? Are any projects of this type contemplated by AID? By the MDBs?

Answer. AID in the past has generally worked through U.S.-based NGOs. A number of these programs have components involving the training of indigenous NGOs in a range of fields. The MDBs generally work with international NGOs. The African Development Bank, with the assistance of several U.S. NGOs, has launched a pilot environmental program which involves working with and training indigenous NGOs.

ENVIRONMENTAL PROBLEMS IN EASTERN EUROPE

Question. As the State Department has taken a major role in coordinating substantially increased flows of technical and financial assistance to the nations of Eastern Europe, what mechanism for planning and coordination has the Department established to ensure that all federal agencies operating in Eastern Europe have as a primary goal of their programs environmental restoration, protection, and enhancement? What specific steps are you taking to ensure that all private-sector joint ventures funded by federal agencies meet environmental standards no less stringent than those applied in this country? What specifically are you doing, in cooperation with AID, to help these Eastern European countries develop strong programs, policies and institutions for environmental protection and restoration?

Answer. The President has appointed Deputy Secretary of State Eagleburger as Coordinator of East European assistance. The Chairman of the Council of Economic Advisors, Boskin, and Deputy Secretary of Treasury, Robson, serve as Deputy Coordinators for this initiative. We have established an environmental assistance working group to facilitate interagency discussion of these issues. This interagency working group includes representatives of the Environmental Protection Agency (EPA), Department of Energy (DOE), the Agency for International Development (AID), Department of Interior (DOI), Department of Commerce (DOC), and the U.S. Information Agency (USIA).

We will consider appropriate environmental safeguards when funding joint venture projects; however, ultimately, every nation will insist on setting its own environmental standards.

To answer the latter part of your question, I would like to refer you to AID Deputy Assistant Administrator Eugene Chiavaroli's testimony before the House Subcommittee on Transportation and Hazardous Materials on April 23, 1990. In his testimony, Mr. Chiavaroli stated that under the policy guidance of the President's Coordinator of Assistance to Eastern Europe, Deputy Secretary of State Eagleburger, AID, EPA, and DOE have held a series of ad hod discussions with key East European environmental specialists, U.S. environmental non-governmental organizations (NGOs), the private sector and other donors concerning future environmental programming in Eastern Europe. AID has been able to play a leadership role among other countries in supporting international environment and environmentally sound energy programs throughout the world. AID provides leadership in environmental management, urban and industrial pollution, energy, forest management, developing local environmental NGOs, and economic analysis and policy reform on environmental issues. They promote environmental institution building, mobilize private investment development, promote technology transfer and applied research, and create a coalition of public, private, and non-government resources to address environmental problems.

As indicated above, AID, EPA, and DOE work together with other relevant agencies under the policy guidance of the Coordinator. The interagency working group has agreed on an overall approach for the Section 703 report and is developing an environmental strategy for Eastern Europe to ensure the effective implementation of the SEED Act.

Question. Given that an estimated $80 billion is needed to address environmental problems in Eastern Europe, and that Western Europe and Japan have indicated their intention to commit billions of dollars worth of aid and assistance to Eastern Europe's emerging democracies, how does the Administration's proposal respond to this need? What needs could the United States most effectively target, and in what manner might these objectives be pursued?

Answer. Environmental assistance is one of the four major categories of support for Eastern Europe proposed in the President's initiative and elaborated in Deputy Secretary of State Eagleburger's testimony before the House Foreign Affairs Committee on March 7, 1990. As part of the initiative, the Administration's plans include the funding of environmental projects in FY 1991 consistent with the $40 million three-year authorization under the SEED Act of November 1989 which authorizes assistance to Hungary and Poland. As Deputy Secretary Eagleburger noted in his testimony, our project to establish the Regional Environmental Center in Budapest is part of this effort. The President's initiative also seeks authorization to extend assistance to the other countries of Eastern Europe making progress toward political and economic reform.

We are currently coordinating with EPA, DOE, AID, and other appropriate federal agencies, as well as with non-governmental organizations, to compile a comprehensive assessment of environmental needs and priorities for Central-Eastern Europe. As we continue consultations with the various countries of the region, we expect to gain a better understanding of more specific environmental needs of these countries.

Our strategy calls for building in FY 1991 on what we start in FY 1990, focusing on technical assistance, training, and limited demonstration projects and using a regional approach to U.S. assistance with some country-specific initiatives. We plan to use the Regional Environmental Center, for example, in promoting regional environmental planning and to supplement/complement these efforts through bilateral and multilateral efforts. In doing so, we will take into account assistance provided by other governments and multilateral organizations.

Question. Given that other Western nations' commitments are so much larger than ours, how does this affect the United States' ability to influence other nations to strengthen their environmental protection efforts?

Answer. The need to strengthen environmental protection efforts has already been recognized by emerging democracies in Eastern Europe. The challenge for the United States and others will be to provide the technical assistance and training needed to serve as a strong foundation for sound environmental planning, both in the short term and long term. The Administration is seeking means to mobilize greater financial resources from the private sector and other donors, as well as to strengthen East European countries' economic capacity to better help themselves environmentally. Eastern Europe's needs will require all the resources that potential donors can provide.

Question. Could we improve the effectiveness of our assistance by providing fellowships to train pollution control "technicians" in the United States?

Answer. This is certainly a possibility and is something we are considering in the Administration's environmental assistance strategy. As you know, however, it is the Administration's policy that funds authorized or approved for FY 1991 should not be earmarked for any particular program, country, or agency. We need the flexibility to respond to the needs of the emerging democracies as these needs become better defined.

One of the primary functions of the Budapest Regional Environmental Center which is scheduled to open sometime during Summer 1990 will be to facilitate environmental education and training and information exchange, as well as linking needs with resources. Although the Center is not intended to be a research facility, it will facilitate and support collaborative environmental activities among individuals and organizations that have the expertise to develop or implement solutions to environmental problems in the region. We expect to have a better idea of how we might provide this kind of assistance when the Center becomes operational this summer. In addition, the Administration and the U.S. private sector are exploring means to provide training opportunities in pollution reduction.

Question. Given the geographic proximity of Europe's borders and the fact that rivers typically run through several countries, are adequate efforts (United States or other) being made to address pollution through a regional or watershed approach? Could U.S. technical assistance facilitate such an approach to environmental management?

Answer. We certainly recognize that pressing transboundary pollution problems are among the most challenging of Eastern Europe's environmental concerns. Our plan is to provide technical assistance and promote environmentally sound policies with a regional approach keeping these transboundary issues in mind. We are considering working with the Poles on their World Bank watershed project in Poland and are exploring efforts which might fit into this framework.

Question. Could you comment on the desirability or need for the United States to establish an international training institute for pollution control technologies?

Answer. The idea is interesting, but an analysis would have to be undertaken to determine its feasibility. This idea should be held in abeyance until the report of the Administration's International Environmental Technology Transfer Advisory Board (IETTAB) is completed.

Question. What actions have already been taken to meet the objectives of the SEED Act?

Answer. The Administration is moving rapidly to implement the environmental objectives of the SEED Act. Approximately $3 million were transferred by the Agency for International Development (AID) to the U.S. Environmental Protection Agency (EPA) to establish the Regional Environmental Center in Budapest and to install an air quality monitoring system and improve drinking water quality in Krakow. Under the auspices of the EPA, and with the support of AID, the United States and Hungary have developed a draft charter and operational guidelines for the establishment of the Regional Environmental Center for Central and Eastern Europe. We anticipate that the center should open sometime this summer.

The Regional Environmental Center in Budapest is an important component of U.S. environmental assistance in East-Central Europe. It is intended to address the environmental challenges common to East-Central Europe. These challenges include severe air, water, and soil pollution; inefficient use of energy; an outmoded industrial base; health problems resulting from environmental degradation; pressing transboundary pollution problems; and a shortage of technical and managerial expertise on environmental issues.

EPA is currently consulting with the Poles to transfer and set up the equipment for an air monitoring network and for improved water quality in Krakow. EPA's clean air strategy for Krakow calls for setting up a minimum of six air monitoring stations in the city, and providing training for technical personnel responsible for operating the equipment. Realistically, the earliest we can begin to ship and install equipment—i.e., air monitors, hardware for the water treatment plants, etc.—is November/December 1990. EPA has identified equipment needs and will shortly finalize plans relative to siting, training, and other related issues.

The Department of Energy (DOE) recently signed an agreement with the Poles to retrofit an existing coal-fired power plant in the city of Krakow with U.S. clean coal technology and to jointly conduct an analysis to define specific activities for an equipment assessment project. DOE and Polish officials have agreed that the activities defined will address low stack pollution in Krakow.

DOE is planning a series of energy conservation seminars to be held in three major cities in Poland this summer. Key officials and plant managers will be invited to these seminars which will focus on some of the U.S. energy conservation programs and technologies. If these seminars are successful, they may be repeated in other East European countries. Although these seminars are not being carried out under the SEED Act, they should aid us in our SEED objectives.

The Administration has also established the International Environmental Technology Transfer Advisory Board (IETTAB), a high-level advisory committee chaired by William Ruckelshaus. The purpose of the Board is to advise the Administration on the feasibility of transferring environmental technology to developing countries and Eastern Europe. The IETTAB will have specific recommendations by Fall 1990. Like the DOE seminars noted above, although this initiative is not being carried out under the SEED Act, recommendations of the Board should aid us in our SEED objectives.

Question. Could you apprise us of the preliminary findings and recommendations already developed for the 1991 report to Congress?

Answer. The Administration views its responsibilities under the reporting requirements of Section 703 as a key exercise in the formulation of the U.S. Government's strategy for environmental assistance to Eastern Europe. As you know, this report is due to the Congress not later than January 31, 1991.

We are improving our understanding of the environmental situation in a technical sense. The efforts of EPA, AID, and DOE in Poland and Hungary are creating an informal cadre of U.S. specialists on Eastern Europe familiar with different aspects of the environmental crisis there. The methodology of integrating various types of data into a comprehensive assessment of environmental needs and priorities is already well developed. We will continue to work with EPA, DOE, AID and other appropriate agencies, as well as with non-governmental organizations, multilateral organizations and the appropriate foreign governments to compile the remaining information needed for the President's report. The resulting recommendations will provide a valuable blueprint for further U.S. environmental assistance efforts in the region.

ENVIRONMENTAL PROBLEMS IN CHINA

Question. Where internal policies (e.g. on air pollution, water conservation, etc.) have broad global or regional implications, what is the U.S. policy on trying to influence such policies? How does this influence make itself felt in countries such as China, which are currently receiving little or no bilateral aid from our government? Are there ways to expand U.S. influence on the internal policies of other nations where such policies affect global concerns—even where no bilateral aid is given?

Answer. In cooperative projects in health, air and water quality, and climate change, U.S. scientists have worked with Chinese counterparts to expand our understanding of the natural environment. By supporting international scientific symposia throughout the world and numerous bilateral exchanges involving Chinese scientists and scholars, the United States has been able to facilitate people-to-people scientific contacts, provide instruction and research opportunities in environmental fields, support efforts to protect the environment, and ultimately to influence how other nations treat the world around us.

We believe that the open sharing of knowledge between United States and Chinese scientists results in positive influence in PRC environmental policy and is the most productive way in the long term to expand U.S. influence on Chinese environmental policies.

Consistent with current United States policy on international financial institutions' assistance to China, we have supported aid for China in areas of basic human needs, including environmental protection. The United States supported a $300 million International Development Association credit, which was approved in May, for forestation in fifteen provinces in China. The project responds to desertification and environmental degradation in some of China's poorest areas and will provide fuelwood and housing materials for the peasant population.

Question. Some might argue that in spite of China's political turmoil and civil rights records, it would still pay to cooperate with China on environmental problems. What are current U.S. programs to assist China, if not with aid, then with information regarding environmental protection? Has China been active in international environmental forums, and if so has it played a constructive role?

Answer. Preservation of the natural environment is a global problem requiring a global response. Clearly, given the size of its land mass and population, China's active participation in preservation efforts is essential to a solution to worldwide environmental problems.

U.S. environmental efforts in China have been in cooperative research activities and in the exchange of technical information, rather than in direct aid. The U.S. Environmental Protection Agency (EPA) and the PRC National Environmental Protection Agency (NEPA) cooperate in many varied projects in the area of environmental protection under the terms of our bilateral Science and Technology Agreement. Both the EPA and NEPA would like to continue and broaden their cooperation, which has been productive and beneficial to both sides. Current cooperative activities cover a broad range of environmental projects including health, air and water quality, and climate change.

In the health area for example, EPA and NEPA are engaged in several multi-year cooperative research projects. One important project is devoted to determining lung cancer risks due to air pollution from coal burning. Another project designed to determine the effects of urban air pollution on children's lungs is in the final planning stages. These projects will increase Chinese and U.S. understanding of the human costs of environmental pollution and may, over the long term, lead to improvements in environmental conditions in China.

In the area of air and water quality, cooperative research projects are underway using technical models to study metal interactions at organic matter surfaces. Knowledge gained in this project will be essential for developing waste handling options as well as increasing our understanding of how metals are transported in groundwater and how exposure to toxic metals affects humans.

Climate change is another area where United States-Chinese cooperative research may contribute significantly to efforts to solve a global problem. The EPA is currently in the initial stages of planning a research project with Chinese scientists on the causes and effects of ozone depletion and to exchange information about applications technology for chlorofluorocarbons (CFC) substitutes.

Although China has not signed the Montreal Protocol on Substances that Deplete the Ozone Layer, the Chinese participate in several international environmental fora. China is an active member of the Intergovernmental Panel on Climate Change (IPCC), co-chairs its Energy and Industry Subgroup and has coordinated an assessment of IPCC's Public Education and Information implementation measures.

China is also a member of the Convention on International Trade in Endangered Species (CITES) and the U.N. Food and Agriculture Organization's Committee on Fisheries.

Question. After the British declared a 6 month reservation on behalf of Hong Kong for the listing of the African elephant under Appendix I of CITES, the Director of the Kenyan Wildlife Service, Dr. Richard Leakey, called the decision "a stab in the back for everyone concerned." He claimed that it gave the signal to poachers that the season was still open. Some observers have claimed that Hong Kong wants to sell its surplus stock to dealers in China. Does the State Department have any information about these plans? The PRC signed CITES in 1981. Are its dealers able to acquire these tusks legally under the treaty, given the Hong Kong reservation? Is the Chinese government working to prevent these shipments, whether or not they are legal?

Answer. The CITES Secretariat has informed the Parties to the Convention that Hong Kong exported 6420 kilograms of elephant ivory to China between October 19, 1989 and January 18, 1990, when the Appendix I listing of the African elephant took effect. Figures since that time are not yet available. It is likely, however, that further ivory shipments from Hong Kong to China have occurred.

Since China has also entered a reservation to the Appendix I listing of the African elephant, shipments of ivory from Hong Kong to China are allowed under CITES, until the UK reservation on behalf of Hong Kong expires on July 18, 1990 or until China withdraws its reservation. Since the Chinese government entered a reservation to the elephant listing, and since CITES allows reserving parties to trade in a given species with non-parties or with other reserving parties, it is not anticipated that the Chinese government will prevent such shipments.

Question. Before the massacre in Tiananmen Square, China had a fledgling environmental movement. Among its leaders was He Bochuan, a philosophy professor in Guangdong; the movement also included many intellectuals and scientists. Among their first targets was the Three Gorges Project to construct the world's largest dam and result in the forced migration of hundreds of thousands of people who reside in areas that would be flooded by rising water. The crackdown has driven this movement, if not into hiding, then at least into silence. What information does the State Department have on the present status of the members of the movement, such as Professsor He? Have members been jailed? What steps, if any, are being taken to convey American concern about such people to the Chinese Government?

Answer. We have no independent information confirming the reported arrest of Professor He. Accurate information on the numbers of Chinese citizens arrested in the wake of the democracy demonstrations, the identity of those arrested, and the disposition of their cases is extremely difficult to obtain.

Since the Beijing massacre, senior Administration officials have raised a range of critical human rights issue in discussion with Chinese leaders. We have consistently called for the release of all those detained for the peaceful expression of political views. The Chinese Government is well aware of our views, both on the general issue of freedom of expression and on specific cases.

ANTARCTICA ENVIRONMENT ISSUES

Question. The background and rationale for each of the three countries now opposing CRAMRA are different. Please describe their positions.

Answer. The Convention on the Regulation of Antarctic Mineral Resource Activities (the Antarctic Minerals Convention) was adopted in June, 1988 by consensus of the treaty countries that were then Antarctic Treaty Consultative Parties (ATCPs). That consensus included New Zealand, Austrailia and France.

Australia and France have since indicated a change in their positions. With respect to New Zealand, it is our understanding that New Zealand does not oppose the Convention, the Government of New Zealand has informed us that it continues to support the Convention, and will seek to play a moderating role in removing objections to it. In the meantime, it has indicated that it will not seek ratification of CRAMRA in the next few months because it wishes to put all its effort behind the preparations for the Santiago meetings 1990 on comprehensive measures for the environment and the elaboration of a liability protocol.

In May, 1989, Australia announced that it had decided not to sign the Antarctic Minerals Convention and would instead work for designation of Antarctic as a wilderness reserve in which all mineral resource activities would be permanently banned. In addition, it called for a comprehensive convention for the protection of the Antarctic environment.

In October, 1989 at the Fifteenth Antarctic Treaty Consultative Meeting (ATCM XV) in Paris, France joined Australia in putting forward a proposal for a comprehensive convention which would establish Antarctic as a "natural reserve/land of science". In a related working paper, they outlined a number of possible components for such a comprehensive convention. Basically, the paper suggests that the convention include general principles regarding comprehenisve protection of the Antarctic environment, types of activities to be regulated and appropriate protective mechanisms and proposed that institutions be set up to implement these principles (an environmental commission, a scientific and technical committee and an arbitration body, assisted by a secretariat and an inspection and monitoring corps).

There was little support for the Australian-French proposal. The great majority of the Antarctic Treaty Consultative Parties (ATCPs) endorsed the approach of building upon the components of the Antarctic Treaty system, and the measures elaborated pursuant to it, to create a comprehensive system for ensuring the protection of the Antarctic environment.

Opposition to the Australian-French proposal reflected several perceptions. First, it was widely viewed, and was so characterized by France and Australia, as aimed at replacing the Antarctic Minerals Convention. The majority of the ATCPs, including the U.S., expressed continued support for the minerals convention and considered it as a key element in comprehensive measures for the protectection of the Antarctic environment. (Seventeen of the twenty-five ATCPs have signed the Antarctic Minerals Convention.)

Second, the majority of the ATCPs, including the Unites States, expressed support for the already extensive network of environmental protection which has been developed within the Antarctic Treaty system. This system comprises agreed recommendations under the Antarctic Treaty, including the Agreed Measures for the Conservation of Antarctic Fauna and Flora; the Covention on the Conservation of Antarctic Seals; and the Convention on the Conservation of Antarctic Marine Living Resources, as well as the Antarctic Minerals Convention.

Third, the Australian-French proposal, as presented, was seen as undercutting the Antarctic Treaty, itself, which has provided a unique and successful international legal mechanism for dealing with activities in Antarctica and for protecting its environment.

Question. Bills have been introduced in the House and the Senate promoting the creation of a world park in Antarctica. Would such a park be compatible with this treaty? If not, what would be the conflicts?

Answer. In attempting to answer this question, it should be noted that there is no agreed understanding as to what is meant by an Antarctic park. The term, and related expressions ("world park", "wilderness park"; "wilderness reserve"), have been used to refer to a number of objectives ranging from stricter regulation of activities in Antarctica to a ban on mineral resource activities or even a prohibition of all human activities there.

In addition, Australia and France, at the Fifteenth Antarctic Treaty Consultative Meeting (ATCM XV) in Paris, October 9–20, 1989, put forward a proposal for a comprehensive environmental convention including designation of Antarctica as a "natural reserve/land of science". Though the proposal does not specifically mention mineral resources, it has been linked with the call for a permanent ban on mineral resource activities in Antarctica put forward by Australia in May, 1989.

In consequence, probably the most common perception of an Antarctic park is that it involves a permanent ban on mineral resource activities as called for by Australia. This proposal for a ban has received little support among the Antarctic Treaty Consultative Parties (ATCPs). Seventeen of the twenty-five ATCPs have signed the Antarctic Minerals Convention (Argentina, Brazil, Chile, China, Finland, German Democratic Republic, Japan, Korea, New Zealand, Norway, Poland, South Africa, Sweden, U.K., U.S.S.R., United States and Uruguay). These Parties, at ATCM XV in Paris, opposed the Australian-French proposal for a comprehensive convention because, inter alia, it was seen as an effort to set aside or replace the Antarctic Minerals Convention. France, Belgium and Italy have supported the proposal for a comprehensive convention, without addressing the question of a ban directly. (Belgium has enacted domestic legislation prohibiting Belgian nationals from undertaking mineral resource activities in Antarctica; the Italian Parliament has passed a non-binding resolution opposing the Antarctic Minerals Convention.) The remaining ATCPs (the Federal Republic of Germany, India, Peru and Spain) have not taken a position.

The lack of support evidenced in Paris for the Australian proposal for a ban is itself one indication of its infeasibility. Institution of this proposal would require a consensus of the ATCPs. Since such consensus seems unlikely, there is concern that the Australian initiative could result in the lack of an agreed basis for determining the acceptability of mineral resource activities in Antarctica—with the future possibility of unregulated or, at best, inadequately regulated activities. With respect to the substantive workability of the Australian proposal for a ban, most ATCPs view the Antarctic Minerals Convention as a more viable basis for dealing with the possibility that commercial activity might emerge in the future. Three reasons appear to underlie this attitude.

First, the concept of a permanent ban is misleading. Even if there were the necessary consensus of the ATCPs to declare a ban, it would be permanent only so long as individual ATCPs continued to support it. The Antarctic Minerals Convention would prohibit consideration of exploration for and development of mineral resources in any area of Antarctica unless there were consensus of all decision-making Parties to the Convention that such activities could accord with the Convention's environmental standards.

Second, the ban would purport to decide for all time that mining in Antarctica could not take place in an environmentally acceptable fashion, regardless of future facts and circumstances. The Antarctic Minerals Convention provides that a determination of the acceptability of mining should be made only if and when interest in such activities emerge, in light of the facts and circumstances at the time and against the rigorous environmental standards and procedures included in the Convention.

Third, if a consensus were to emerge that mineral resource activity should be considered in Antarctica—however unlikely that event seems now—the Antarctic Minerals Convention would provide an agreed and rigorous process for structuring such consideration. The "permanent" ban, if broken or lifted, would offer no such safeguards. The worst circumstances in which to seek to negotiate an agreed process for considering mining would be after commercial interest in it had become widespread.

The Parties to the Antarctic Treaty at ATCM XV considered the question of comprehensive measures for the protection of the Antarctic environment, an item proposed by the delegation of Chile. They agreed to set as a priority objective "the further elaboration, maintenance and implementation of a comprehensive system for the protection of the Antarctic environment and its dependent and associated ecosystems . . ." The United States, Australia and France—and all Treaty Parties—endorsed and share this objective.

The United States and the majority of the ATCPs believe that such a comprehensive system should build upon the extensive network of environmental protection already elaborated within the Antarctic Treaty system, including the Antarctic Minerals Convention.

A system of protected areas will be an important part of the comprehensive system for protection of the Antarctic environment to which the Treaty Parties have committed themselves. Under the Agreed Measures for the Conservation of Antarctic Fauna and Flora (1964), Antarctica has been designated as a Special Conservation Area within which the taking of native species is prohibited, except for strictly defined scientific or subsistence purposes. Provision has also been made for setting aside areas of special ecological significance and areas of particular scientific value—Specially Protected Areas (SPAs) and Sites of Special Scientific Interest (SSSIs), respectively. There are currently 19 SPAs and 31 SSSIs, designated by the Treaty Parties. In addition, over 50 historic sites and monuments have been designated.

Action was taken at ATCM XV to extend the protected area system in Antarctica in significant degree. The Treaty Parties agreed to provide for the designation of two new categories of protected area: first, Specially Reserved Areas (SRAs) to protect areas of outstanding geological, glaciological, geomorphological, aesthetic, scenic or wilderness value; and second, Multiple-Use Planning Areas (MPAs) to provide means for coordinating human activities in areas where such activities pose risks of mutual interference or cumulative environmental impacts.

The Antarctic Protected Areas system, as it has evolved, provides for setting aside areas or parks for a wide variety of environmental and scientific purposes.

Question. The grounding, and subsequent oil spill from the *Bahia Paraiso* near Palmer Station on the Antarctic Peninsula demonstrated the difficulty in responding to oil spills in the Antarctic. How does the current ATS structure deal with environmental disasters of this type? What lessons were learned from this unfortunate event, and what policy and management changes have been made to reduce both the risk and consequences of future spills?

Answer. The Parties to the Antarctic Treaty have committed themselves to actions to prevent and mitigate marine pollution in the area of the Antarctic Treaty. In this effort, they have sought to learn the lessons from the unfortunate grounding of the *Bahia Paraiso.*

At the Fifteenth Antarctic Consultative Meeting (ATCM) held in Paris in October, 1989, the United States presented a paper describing a comprehensive approach to marine pollution issues in Antarctica. As a result of the U.S. initiative, the meeting adopted recommendation XV-4, which is attached. The Recommendation calls for Governments to take measures within their competence to prohibit within the Antarctic Treaty area certain discharges and disposal from vessels and to ensure that their vessels comply with the relevant provisions of specified international Conventions on vessel safety and pollution control. It also calls upon them to become parties to these conventions if they are not. In addition, it calls for the establishment of contingency plans for marine pollution response and sets forth a procedure for doing so.

The prohibitions contained in the Recommendation XV-4 on discharge or disposal of certain wastes within the Antarctic Treaty area are consistent with designation of the area as a special area under the 1973-78 International Convention for the prevention of Marine Pollution from ships (MARPOL 73-78). Therefore, the meeting agreed that the Contracting Parties to the Antarctic Treaty that are also parties to MARPOL 73-78 consider formally doing so within the International Maritime Organization (IMO). We are now consulting with Antarctic Treaty Parties in this regard.

The meeting further agreed that issues related to liability for marine pollution damage warranted attention, as well as consideration of the relevant of additional international conventions to questions of marine pollution in Antarctica. In this context, specific mention was made of further restrictions on dumping and incineration at sea in the Antarctic Treaty area, pursuant to the London Dumping Convention; considering designation of the Antarctic Treaty area as a special area under Annex II of MARPOL 73-78 on transport of chemicals in bulk; and the 1989 Convention on Control of Transboundary Movement of Hazardous and Their Disposal. Attention was called to the hazards of vessel operation in the Antarctic Treaty area and the view expressed that it would be useful to consider special requirements for vessel construction in the future.

Finally, it was agreed that the organizers of the next ATCM should convene a meeting of experts to discuss contingency plans for marine pollution response.

In addition to these steps on the specific problems of marine pollution, ATCM XV also agreed to organize a special meeting of Antarctic Treaty Parties to discuss comprehensive environmental measures. It will be held in Santiago, Chile, in November, 1990, and its goal is the "further elaboration, maintenance and effective implementation of a comprehensive system for the protection of the Antarctic environment".

With specific regard to the wreck of the Argentine vessel, *Bahia Paraiso* U.S. Government officials continue to consult with Argentine officials over the possible disposal of the vessel.

Question. The *Bahia Paraiso* was a tourist ship. Does the event suggest a need for stricter oversight of the tourist industry? How can oversight occur when the ship is not under U.S. registry? What actions are being taken with other ATCPs to regulate tourism? To what extent do tourist visits disrupt the research activities of the scientific stations? How might these disruptions be minimizeds or avoided?

Answer. In our view, the Antarctic Conservation Act (PL-95-541) establishes the necessary authority for regulating tourist activities by United States citizens in Antarctica. Tourist activities in Antarctica are subject to a number of significant measures adopted by the Parties to the Antarctic Treaty pursuant to Article IX of the Treaty. These measures recognize that effective regulation of activities in Antarctica, such as tourism, requires international action. Many of these measures contain environmental regulations designed to apply to all activities in Antarctica, including tourism. The far-reaching steps on marine pollution and waste disposal agreed by the Treaty Parties at the Fifteenth Antarctic Treaty Consultative Meeting in October, 1989 are good examples of this functional approach.

Questions regarding the effect of tourist visits on research activities at U.S. scientific stations are probably best addressed to the National Science Foundation (NSF), which runs the U.S. Antarctic Program. However, it is our understanding that NSF is working directly with tour groups to minimize their disruption to U.S. scientific efforts.

SUBMITTED TO DEPARTMENT OF THE TREASURY

U.S. PARTICIPATION IN WORLD BANK ENVIRONMENTAL GRANT PROGRAM

Question. A February 1990 report on Funding for the Global Environment by the World Bank noted that the Bank administers a technical assistance grant program for the environment, with initial funding from Japan and later supplemented by contributions from Denmark, France, Norway and Sweden. Bank sources indicate the fund is about $27 million and is used for technical assistance to build institutional capacity in developing countries, assisting them with better environmental and/or natural resources management capability.

In some cases, the donors make contributions to this grant program by using funds from their bilateral overseas development assistance agencies. Why is the United States not participating in the funding of this program? Is funding for the program being considered by AID?

Answer. I can not speak for the Agency for International Development or why it has not yet provided funding specifically for this purpose or whether or not it is considering such funding. I do know that there are a number of different cooperative funding arrangements now in existence between AID and the Bank for various environmental purposes, including promotion of energy efficiency and conservation. In addition, the Trade and Development Program has provided about $500,000 to the Bank for project preparation work related to the environment, specifically for pollution control and hazardous waste management.

Question. One problem that is often cited by the MDBs in developing effective integration of environment into policies and projects in specific sectors like energy, transport, urban and industrial development and others is that the priority for environment is low in many developing countries, often because they lack effective environmental institutions. Would it not be beneficial to these countries—and to the furtherance of environmental priorities in MDB programs—to encourage environmental institution building through a grant program such as this one?

Answer. From Treasury's perspective, it would certainly be beneficial to encourage environmental institution building in many of the developing countries, particularly in environmental impact assessment, but also in other areas, through such a grant program. I can not speak, however, on how such a funding proposal would fit into AID's overall funding priorities.

Question. The United States has taken a leadership role in pushing the World Bank to put a higher priority on environmental protection and management. Doesn't our failure to participate in positive programs like this one reflect on our environmental exhortations in other areas?

Answer. The United States has taken the leadersship role in this area in all of the multilateral development banks. I agree that the provision of funding for such a grant program would be helpful in achieving our environmental objectives and that it would give greater weight to our overall efforts to bring about greater environmental reform. However, I do not know that our overall efforts have been harmed by the lack of such funding at this point.

GENERAL ENVIRONMENT AND CONSERVATION ACTIVITIES OF MDBs

Question. The World Bank has stated that it has completed Environmental Issue Papers (EIPs) for its most active borrowers and that it is working on Environmental Action Plans for 30 countries. Are you aware of the countries for which such documents have been prepared?

What countries have been the subjects of these EIPs.

Are these documents available to organizations and individuals outside the World Bank, such as local or international nongovernmental organizations or U.S. government officials? At what stage of development are these documents to be made available? Are "preliminary" reports available?

If not, has the Bank established a way to separate and make available environmental impact information from the more sensitive country development information that it believes must remain confidential?

Answer. The Bank has prepared EIPs for all borrowing countries. However, we understand that these vary greatly in degree of detail and analysis depending on the level of Bank activity in the country. The EIPs are documents for internal bank guidance and serve as the basis for preliminary policy dialogue on environmental issues. They are not generally available to the public. However, in some cases, they have been made available to NGOs upon request. The Department of Treasury has seen samples.

The Bank's new operational directive on environmental impact assessment (EIA) directs its borrowers to consult NGOs and affected groups in the assessment process and to make as much information available as possible. In the IDA replenishment negotiations, the United States obtained language requiring borrowers to release EIAs at least 120 days in advance of Executive Board presentation. The Bank would make the EIAs available to members of the Executive Board of Directors at the same time.

Question. The World Bank has also noted that 30 major environmental projects are expected to be approved by the Bank Board. Please give us examples of these projects. Can you give examples of specific projects that have been changed as a result of environmental concerns?

Answer. The World Bank Board recently approved projects to Brazil and the Central African Republic for natural resource management. The Brazil project covered institutional strengthening of environmental agencies, creation of new protected areas, and rehabilitation and protection of several endangered ecosystems including tropical forest areas and wetlands. The Central African Republic project covered policy changes pertaining to the forestry sector, radical restructuring of the forestry management agencies, forest inventories, and pilot projects involving wildlife management and forest conservation.

A Bank project for the Amazon region of Bolivia was changed extensively as a result of U.S. expression of concerns very early in the project cycle and involvement of international and lcoal NGOs. The project has switched from a focus on large farms to assistance to the small-holders who have migrated to the region. The objective is to direct settlement to those areas most suitable for agriculture (backed by soil surveys) and to encourage the development of sustainable agriculture in fixed areas so as to limit deforestation. The development agencies in the area will benefit from institutional strengthening. There is also an Amerindian protection and development component which will be implemented with the sustantial involvement of a Bolivian NGO. The entire project will be subject to monitoring by an independent panel consisting of members of the Bolivian Academy of Science, local and internationl NGOs.

Question. In 1987, Congress directed the Secretary of Treasury to instruct the U.S. Executive Directors of each MDB to identify procedures to "include assessments of the benefits and cists of environmental impacts and possible mitigating measures" associated with their projects (H.R. 3750, enacted into law by H.J. Res 395, Sec. 1306 (a)). Last year, in a report to Congress, Treasury noted that the Banks had not yet developed their own cost-benefit procedures, but that staff could "avail themselves" of guidelines and consultants to assist in preparing cost-benefit analyses.

Have such cost-benefit analyses been prepared for projects and programs under consideration for loans from the World Banks?

Are such anayses routinely made?

Will the Bank adopt its own consistent guidelines to assess the environmental, social and economic costs and benefits for projects funded by the World Bank?

Answer. The World Bank has made the most progress in this area although the Asian Development Bank and the Inter-American Development Bank have also begun work. Cost-benefit analyses do include environmental costs and benefits where these can be quantified. When these cannot be quantified, they are characterized in qualitative terms so that they can be taken into consideration in the project cycle. The analytical basis for quantifying environmental benefits and costs is still not well developed. The World Bank is continuing its research in this area.

Question. In its 1989 report to Congress, "Progress on Implementation of Environmental Reform in the Multilateral Development Banks," Treasury noted that the World Bank would continue to research links between economic growth and environmental and resource degradation.

What has been the progress on the World Bank's efforts to research relationships between environment and economic growth (and poverty), and the potential gains from including conservation policies in structural adjustment decisions?

Is the Bank currently researching the relationship between the traditional formulation of national income accounts and natural resource degradation? Is the World Bank—or other MDBs—actively incorporating natural resources into its formulations of national income accounts.

Answer. Research related to environmental is done in various parts of the World Bank. A number of papers exploring the question of environmental sustainability and economic development have been prepared. Sometimes these relate to specific sectors in particular countries, for example, tropical forests in Brazil. The research is used to guide policy dialogue and, in some cases, project preparation. Several projects in Brazil reflect the work that has been done on tropical forests. Another project in the Ivory Coast was partly based on assessments of the impact of deforestation on growth in agricultural productivity.

The Bank has also used research on environmental issues to incorporate natural resource management components in structural adjustment loans (SALs). SALs in Guinea, Ghana and Papua New Guinea are examples.

The World Bank is doing research on incorporating natural resource parameters into national income accounts. It has begun work on exploring the use of such parameters in Mexico's statistical compilations and expects to prepare a number of other case studies. However, MDBs do not compile national income accounts for countries. These are compiled by the countries themselves, sometimes with assistance from the U.N. Statistical Office. The World Bank is cooperating with the U.N.S.O. on expanding national accounts to include new information.

MULTILATERAL DEVELOPMENT BANKS AND DEBT-FOR-ENVIRONMENT INITIATIVES

Question. Has Treasury instituted any new incentives for commercial banks to donate portions of their debt portfolios to charitable organizations since it adopted IRS Ruling 87-124, which allows commercial banks to write off the full face value of such donations? Is this mechanism being used? If not, what are the obstacles?

Answer. Revenue Ruling 87-124, issued in November 1987, clarified the tax consequences for banks of entering into charitable contributions of debt paper. In particular, the ruling indicated that a donor of debt paper is able to take a tax deduction both for the loss (represented by the difference between the face value of the debt and its fair market value) and for a charitable contribution (in an amount equal to the fair market value of the debt paper). In other words, the ruling made consistent the tax treatment of a bank donation of debt paper with a bank donation of the proceeds of a sale of debt paper.

Banks' decisions about whether to donate debt paper are based on a variety of considerations. While Revenue Ruling 87-124 gave banks a clarification of tax treatment and equal incentive to donate paper as to sell it and donate the proceeds, many banks still view developing country debt paper as a relatively valuable asset which they are not willing to surrender based solely on the tax advantages involved.

In 1989, Treasury supported legislation aimed at making it more attractive for commercial banks to donate developing country claims for development or environmental purposes. In what is now PL 101-240, Congress calls on bank regulatory agencies to adopt uniform accounting guidance that will allow banks to value the LDC loan assets given to charity (i.e., an environmental NGO) at the fair market exchange dollar equivalent of the local currency received as a result of a debt swap transaction. Treasury has encouraged the regulators to act in a timely manner to adopt accounting guidance consistent with the intent of the law.

Question. Has the Treasury Department been successful in incorporating environmental provisions throughout implementation of the Brady Plan? (A report on this is due to Congress by April 15, 1990.)

Answer. The Treasury Department uses its role in the MDBs as the primary tool for influencing developing countries' environmental policies and natural resource management. We have devoted intense efforts to increasing the MDBs' focus on the environment, both as an important factor to be considered in general lending decisions and as an area in need of greater attention in itself. Specifically, we have actively pressed the MDBs to: expand their use of environmental impact assessments and public access to them; develop environmental action plans on a broad basis; build up their environmental staffs; and set up sector lending programs for the environment.

There is more to be done. Environmental issues should be incorporated more fully into the policy dialogue the MDBs pursue with developing countries. Environmental action plans and impact assessments are critical tools for this process, and the MDBs must be further urged to develop them on a broader basis.

Because we believe that debt-for-nature swap transactions can help leverage funds to support environmental projects and sustainable resource management in developing countries, we are seeking to expand the role of the MDBs in facilitating these swaps. For instance, we are encouraging the use of a portion of environmental sectoral or project loans to finance debt-for-nature swaps. The prospect of debt reduction through such transactions, even if limited in nature, should offer an incentive to debtor countries to work with the MDBs in this area.

Strengthening the MDBs' focus on the environment through these measures is the way to establish a productive link between a country's willingness to pursue environmentally sustainable development and the international community's support for efforts to reduce debt burdens. Any stricter linkage could delay or undermine international efforts to provide needed financial relief in support of economic reforms aimed at establishing strong economic growth. Our aim is to ensure, both by supporting economic reform programs and urging the broader incorporation of environmental concerns into these programs, that such growth is both economically and environmentally sustainable. While we believe that a debt-for-nature swap option (either through a commercial bank donation of debt or a cash buyback linked to environmental commitments) could be a feasible option within commercial bank financing packages, we have never intervened in debtor/commercial bank negotiations to insist on specific options, nor do we believe it would be appropriate to do so.

[CLERK'S NOTE.—The Department of the Treasury did not respond to three other questions on MDBs and debt-for-environment initiatives.]

SUBMITTED TO THE AGENCY FOR INTERNATIONAL DEVELOPMENT

INCREASING ENVIRONMENTAL STAFF AT A.I.D.

Question. Give me a detailed accounting of how A.I.D. intends to comply with PL 101-167, in terms of increasing the environmental staff at all levels.

Answer. So far this year, A.I.D. has established a total of 18 positions in response to the legislation. Sixteen of these are devoted to environmental concerns. The positions are located in the field and in the regional and technical offices of A.I.D./Washington.

The four field positions are:
Global Warming Advisor (Mexico);
Global Warming Advisor (Brazil);
Environmental Specialist, Foreign Service National (Bangladesh);
Regional Land Use and Environmental Planner (PRE/Housing Jamaica).
The seven regional bureau positions are:
Global Warming Advisor (LAC Washington);
Environmental Project Manager (ANE Washington);
Natural Resources Economist (ANE Washington);
Environmental Program Manager for Eastern Europe (ANE Washington);
Industrial Pollution Specialist (ANE Washington);
Natural Resources & Energy Policy Advisor (AFR Washington);
Global Climate Change Advisor (AFR Washington);
The seven remaining positions are in the central bureaus, as follows:
Environmental Training Specialist (S&T/Energy);
Environmental Specialist (S&T/Energy);
Global Warming Advisor (S&T/FENR);
Pest Management Advisor (S&T/AGR);
Animal Agriculture Systems Advisor (S&T/AGR);
Senior Ecologist (S&T/AGR);
Environmental Economist (PRE/Housing Washington);

We expect that the number of positions will grow as project initiatives are developed at the country level during the next two fiscal years. The need for additional highly specialized technical experts in Washington to support the growing field expertise will be met through short or longer term arrangements, as appropriate.

In addition, we are initiating an Agency-wide staff training program to provide a range of environmental training opportunities for A.I.D.'s present staff. Areas to be covered by specific training courses include: environmental impact assessment, natural resources management, and natural resources economics. Additionally, short-term workshops and awareness programs will be provided for Mission Directors and others not directly responsible for project development and implementation.

Question. How many of these positions do you expect to fill with environmental specialists, particularly the kind of specialists who will understand the complexities of biological diversity?

Answer. The Science and Technology Bureau is bringing on board a very experienced biological diversity expert this summer. As the need for additional highly specialized expertise in biological diversity develops in response to project initiatives developed at the country level during the next two fiscal years, we will meet the specific needs through the use of direct hire, IPA, and other available personnel authorities, as appropriate.

Question. How will this translate in the Washington bureaus, for example the Asia/Near East Bureau, where leadership does not seem to be coming from the top?

Answer. The leadership of the Bureau for Asia Near East & Europe (ANE) is committed to addressing environmental concerns within the region, including the serious problems in the emerging democracies of Eastern Europe. Of the 14 positions specified to date for Washington, four are in ANE, one of which is for an environmental specialist for Eastern Europe. Of the four positions specified to date for the field, one is in Asia. We expect that the number will grow as more environmental project initiatives are developed at the country level during the next two fiscal years.

Question. Last year the Committee directed A.I.D. to organize a cadre of U.S. experts from industry, academia, non-governmental organizations and other government agencies capable of providing technical assistance in developing countries concerning energy policy and planning, end-use efficiency and renewable energy. The Committee included authority in the bill to reimburse experts and technicians with program funds in order to facilitate this.

Has A.I.D. expanded the Energy Training Project as directed by the Committee?

Answer. Courses conducted under the Energy Training Project are being modified or expanded to address global climate change issues, and three new courses are being developed to train participants from developing countries.

Before the end of the FY 1990, A.I.D. will award a new training contract to design and implement an environmental training agenda for the Agency. Under this mechanism, the contractor will train up to 100 direct-hire A.I.D. staff each year for the next three years.

Question. Provide for the record your record of staffing increases both directly and indirectly by region and bureaus.

Answer. A.I.D. has taken steps to hire up to 20 experts in end use energy efficiency, renewable energy, and environmental activities, each year for three years. In January, overseas missions and A.I.D./Washington offices were queried about their needs for program-funded environmental positions. A personnel hiring plan was prepared in March to determine how best to meet those needs, within available funds and hiring authority.

Bureaus and offices are moving ahead to specify, establish, and fill environmental positions with qualified individuals. The current status of FY 1990 positions is:

ON BOARD

Industrial Pollution Specialist (ANE Washington);
Natural Resources & Energy Policy Advisor (AFR Washington);
Environmental Training Specialist (S&T/Energy).

BEING ADVERTISED

Global Warming Advisor (Mexico);
Global Warming Advisor (Brazil);
Regional Land Use and Environmental Planner (PRE/Housing Jamaica).

TO BE ADVERTISED

Global Warming Advisor (LAC Washington);
Environmental Project Manager (ANE Washington);

Natural Resources Economist (ANE Washington);
Environmental Program Manager for Eastern Europe (ANE Washington);
Environmental Specialist, Foreign Service National (Bangladesh);
Global Climate Change Advisor (AFR Washington);
Environmental Specialist (S&T/Energy);
Global Warming Advisor (S&T/FENR);
Pest Management Advisor (S&T/AGR);
Animal Agriculture Systems Advisor (S&T/AGR);
Senior Ecologist (S&T/AGR);
Environmental Economist (PRE/Housing Washington).

We expect that the list of positions will grow as project initiatives are devleoped at the country level during the next two fiscal years and are approved throughout A.I.D.

The S&T Bureau is bringing on board a very experienced expert in biological diversity this summer. As the need for additional highly specialized expertise is determined, we take specific actions to meet such needs, using direct hire or other personnel authorities, as appropriate.

A.I.D. ENERGY PLANNING

Question. A.I.D. energy policy appears to be driven primarily by individual country needs rather than by an overall policy or philosophy. Outside witnesses claim A.I.D. policies actively promote increased reliance of fossil fuels and large scale electrical systems to the detriment of renewable or other technologies. In the case of Pakistan, A.I.D. funds an energy planning project, whose principle purpose is to direct further energy development in that country.

Using Pakistan as an example, explain how A.I.D. energy policy:

1. supports local resource development;
2. promote use of energy sources other than fossil fuel
3. improves urban energy development through utility management, energy conservation and model energy privatization programs.

Answer. A.I.D. energy projects in Pakistan, especially the Energy Planning and Development project and the Private Power Generation project, provide technical assistance and training to government agencies and private organizations to help them identify local energy resource options and establish economically and environmentally sound investment programs for their development. Under the Private Power project, viable private energy investment projects for local resource development are eligible for project feasibility support and loan funding.

A.I.D. has supported under the Energy Commodities and Equipment project the importation of renewable energy technologies. As part of its Rural Electrification Project, A.I.D. succeeded in incorporating renewable energy technologies as options for decentralized electricity generation in the Pakistan Rural Electrification Master Plan. The Energy Planning and Development project is promoting the development of small hydro systems. And A.I.D. is encouraging the GOP to consider viable investment proposals from small hydro, solar, biomass and wind energy companies under the Private Power Generation project.

A major focus of the A.I.D. energy program in Pakistan (Rural Electrification project) has been on improving planning, management, and operation of the electric utility, the Water and Power Development Authority (WAPDA) in both generation and distribution. We have provided technical assistance, training and equipment. Energy losses have been substantially improved and the quality of service increased in some locations.

A major new and efficient power plant has been completed and the efficiency and life expectancy of several existing plants has been improved.

Under the Energy Planning and Development project, we have helpd establish a National Conservation Program and Energy Conservation Center, which works with public and private organizations in identifying opportunities (e.g. audits); training managers and operators, e.g. boiler operators, and transfers appropriate technologies (e.g. engine tune-up equipment). A new effort will be started to provide technical assistance and training to energy planners and managers in environmental planning. A.I.D. projects have supported energy conservation and loss reduction investments (Energy Planning and Development project and Rural Electrification project); energy efficient audits, training and feasibility studies (Energy Planning and Development project); and the importation of energy efficiency equipment (Energy Planning and Development project and Energy Commodities and Equipment project).

A.I.D. has been instrumental in setting up a model privatization program for power generation under which the utility (WAPDA) will purchase power from private energy facilities at a negotiated price. A.I.D. is providing technical assistance for this multi-donor supported program, including a long-term environmental specialist.

A.I.D. will also co-finance project development costs with U.S. companies receiving letters of intent from the Pakistan government.

A.I.D. TROPICAL FORESTRY PROGRAMS

Question. In Section 534 of P.L. 101-167, passed last year, A.I.D. is instructed as follows: "In order to achieve the maximum impact from activities relating to tropical forestry, the Agency for International Development shall focus tropical forestry assistance programs on the key middle- and low-income developing countries (". . . key countries") which are projected to contribute large amounts of greenhouse gases related to global warming as a result of industrialization and the burning of fossil fuels, and destruction of tropical forests." Presumably, this provision of law directs A.I.D. to provide forestry aid to countries that were not receiving such aid before, such as Brazil.

In Section 533 of the Act, A.I.D. was directed to "devote at least 10 percent of the resources allocated for forestry activities to the preservation and restoration (as opposed to management for extraction) of natural forests."

Section 533 also directs A.I.D. to "devote increased resources to technical training of mission directors in . . . reforestation and biodiversity."

What countries has A.I.D. determined are "key countries" under the Section 534 provision?

How will A.I.D. change the focus of its tropical forestry programs in order to comply with this provision of law?

Will this require eliminating forestry assistance to countries that were receiving forestry aid, but do not fall into the "key country" category?

Answer. A.I.D. has identified the following "key countries" to be the focus of our global climate change program: Brazil, Mexico, Central America (considered as a single geographic area of focus for these purposes), India, Indonesia, the Philippines, Pakistan, Poland, and Zaire. The composition of this list may change as A.I.D. finalizes its plans. The degree of attention given to energy efficiency versus forestry-related development activities will vary from one country to another.

A.I.D. is moving ahead vigorously with earlier planned forestry initiatives in Central America, the Philippines, and Indonesia and is launching new efforts in improved tropical forest management and conservation in Brazil and Mexico.

A.I.D.'s draft global climate change strategy provides guidelines to field Missions that call for targeting as much as 60 percent of new project starts in A.I.D. forestry programs toward key countries by fiscal year 1994. Regional Bureaus will attempt to meet these targets to the extent possible without eliminating otherwise well-justified and developmentally appropriate tropical forestry assistance work in other countries.

Question. What activities will A.I.D. pursue in spending 10 percent of its forestry resources on preservation and restoration of natural forests?

To what extent does A.I.D. utilize indigenous tree species in its tree planting programs?

If reforestation is to be part of these expenditures, will indigenous species be required or encouraged in order to assure regrowth of species natural to the areas that have been deforested?

Answer. A.I.D. has been giving increased emphasis within its forestry program over the past several years to forest preservation and protection. At the end of fiscal year 1989, three-quarters of all planned new forestry projects contained specific forest protection provisions relating to biological diversity conservation.

The Forest Resources for a Sustainable Environment (FORESTA) project begun in 1989 in Costa Rica is a good example of a forestry development project containing heavy emphasis on forest habitat protection. This project supports protected area management and provides economic development opportunities for local people living in buffer zones surrounding several national parks in the Central Cordillera.

A.I.D.'s tree planting activities are increasingly dominated by participatory agroforestry approaches rather than by large-scale block planting. Locally useful and well-known indigenous tree species are routinely included together with exotics in participatory agroforestry approaches working with small farmers on A.I.D.-financed projects. Local fruit and nut trees and woody fodder shrubs are typically included in the mix of tree species used as a matter of standard practice within such projects.

Question. How will A.I.D. comply with the requirement that increased resources be devoted to training Mission Directors in refoestation and biodiversity? Will this include training in methods of protecting natural forests? Will Mission Directors be expected to place a higher priority on these concerns after receiving such training?

Answer. A.I.D. is launching a new program-funded environmental training program during the current fiscal year for direct-hire employees. The training program content will belnd energy efficiency with forestry and other environmental topics, particularly related to global climate change. Orientation briefings and seminars for Mission Directors and staff will include attention to reforestation, tropical forest conservation, protection and management, and related biological diversity conservation.

A.I.D. has a reasonable expectation that execution of its new environmental training programs for direct-hire employees, including Mission Directors, over the next three years will result in a greater sensitivity and priority to these concerns within country-level assistance programs. These expectations are strongly bolstered by recent trends within A.I.D. in funding for biological diversity conservation. Total obligations for biological diversity rose from $4.8 million in FY 1987 to over $12.0 million in FY 1988 and exceeded $17.0 million in FY 1989.

A.I.D. AND THE GLOBAL WARMING INITIATIVE

Question. Section 533(d)(1) of Public Law 101-167 directs the Administrator of the Agency for International Development to inform its bureaus and missions of its participation in a "Global Warming Initiative." The initiative will emphasize the need to reduce emissions of greenhouse gases through policies consistent with economic development: "This initiative shall emphasize the need to accelerate sustainable development stragegies in areas such as reforestation, biodiversity, end-use energy efficiency, least-cost energy planning, and renewable energy, and shall encourage mission directors to incorporate the elements of this initiative in developing their country programs." Further, Section 533(d)(2) directs A.I.D. to increase its expertise and staff in the energy field, and to provide increased resources for training, planning, reforestation and biodiversity.

Section 534 of Public Law 101-167 expands on the "Global Warming Initiative" and directs A.I.D. to focus tropical forestry and energy assistance programs on countries where assistance would have the greatest impact on reducing the impacts of greenhouse gas emissions.

Is A.I.D. currently funding renewable energy programs?

Answer. A.I.D. supports a variety of projects in developing countries to promote the use of renewable energy. These activities include funding of feasibility studies to evaluate the financial and technical viability of commercially available renewable energy technologies, support for developing marketable renewables products, training and information dissemination, and promotion of private sector participation in electricity generation using indigenous renewable resources. Among current projects are several that focus on the testing, training, and demonstration of renewable energy technologies in Egypt, India, and Pakistan.

Some A.I.D. Missions have also encouraged the application of renewable energy technologies as small parts of other projects. These include: photovoltaics applied to lighting, water pumping, and refrigeration in Botswana, Djibouti, Morocco, Tunisia, and Zaire; small hydro facilities in Liberia and Peru to generate electricity for villages and local small-scale industry, and in Madagascar and Zaire to provide shaft-power for agricultural processing.

Through its projects, A.I.D. funds pre-investment studies of proposed renewable energy projects that employ off-the-shelf technology and have an identified financing source.

A.I.D. is also working in a number of countries including Costa Rica, the Philippines, Thailand, and Indonesia to promote the use of sugarcane, rice residues, woodwastes, and palm oil for power generation, primarily by privately-owned agricultural processing mills.

A.I.D. also focuses on projects to develop solar, wind, hydro, and geothermal resources by cost-sharing site-specific pre-investment studies. Specific projects include geothermal in Central America and Kenya, small hydro in Costa Rica, and promotion of more efficient cookstoves in Central America.

A.I.D. has just published a vendors' catalog of U.S. renewable energy technology suppliers and will soon publish a guidebook on selecting technologies for vaccine refrigeration. A.I.D. will also soon publish, in conjunction with the U.S. Export Countil on Renewable Energy (ECRE), "Renewable Energy Projects in A.I.D.-Assisted Countries."

A.I.D. also funds travel of foreign nationals to attend U.S. industry-sponsored conferences, workshops, and reverse trade missions (visits to the U.S. aimed at exposing foreign nationals to exportable technology, services, or equipment).

In 1989, A.I.D. began a program to train utility planners in "least-cost" planning methodologies that consider renewable energy options and efficiency improvements along with more conventional technologies for utility investments. Initial planning exercises are being conducted in India and Costa Rica.

A.I.D. is also promoting innovative financing for dissemination and servicing of small-scale renewable technologies in the Dominican Republic. The purchase of these commercially available photovoltaic products by rural villagers is financed through a bank designed specifically to finance capital investment of a few hundred dollars at low interest. In 1990, A.I.D. will promote replication of this type of activity in other countries.

Question. Has the agency increased its energy staff since the passage of Public Law 101-167? Is it planning increases?

Answer. So far this Fiscal Year, A.I.D. has established a total of eighteen positions in response to the legislation. Two of these are devoted virtually full time to energy. Both are located in A.I.D.'s Office of Energy in the Bureau for Science and Technology.

A.I.D. expects that staffing will grow as energy programs are developed and approved throughout the Agency, some in specific response to global climate change initiatives. Increased program activity is anticipated from a heightened awareness at all levels of A.I.D. and in A.I.D.-assisted countries that efficient energy is a key component of economic growth and that energy is a priority component of programs that deal with global climate change.

To train and increase the awareness of its own staff (including Mission Directors) A.I.D. is developing an environmental and energy training agenda that includes the training of up to one hundred A.I.D. staff each year for the next three years.

Question. Has the agency determined which countries will be designated to participate in tropical forestry and energy assistance programs? (A report on key countries is expected from the agency by April 15, 1990).

Answer. A.I.D. has tentatively designated the "key countries" which will be the focus of our global climate change program. They are: Brazil, Mexico, Central America (considered as a single entity for these purposes), India, Indonesia, the Philippines, Pakistan, Poland, and Zaire.

These countries have been chosen on the basis of their (1) current or predicted emission of greenhouse gases, (2) ability to be influenced by A.I.D. efforts, and (3) economic vulnerability, e.g., degree of dependence on its coal reserves or forests for continued economic growth or relative economic wealth.

A.I.D. was not able to complete the report by April 15. We now plan to submit the report to Congress by July 15, 1990, per our recent notification to Congress.

A.I.D. and Debt for Environment Initiatives

Question. The recently passed International Finance and Development Act, P.L. 101-240, authorizes the U.S. Agency for International Development (A.I.D.) to assist developing countries with environment and natural resource programs through grants which would be used to purchase a debtor country's debt at a discount. The law also directs the Administrator of A.I.D. to "encourage as many eligible countries as possible to propose such exchanges." This law, as well as the FY 1990 foreign operations appropriations (P.L. 101-167), also allows grantees to collect interest on funds derived from the discounted debt in order to establish ongoing trust funds or other financial mechanisms to fund long-term environment and natural resources programs. A.I.D. participated in at least one debt-for-nature swap prior to the enactment of these laws (August 1989), involving the World Wildlife Fund and the country of Madagascar.

What countries has A.I.D. encouraged to participate in debt-for-nature exchanges? Has there been increased interest from debtor countries and international or locally-based nongovernmental organizations in participating in debt-for-nature swaps with the use of A.I.D. funds?

Answer. In the wake of recent legislative changes affecting debt-for-nature exchanges (P.L. 101-167 and P.L. 101-240), A.I.D. notified its top management and all overseas missions of the provisions requiring A.I.D. to take the initiative in stimulating debt-for-nature exchanges, especially in sub-Saharan Africa.

There has been a modest but growing interest in debt-for-nature exchanges. The provisions of the legislation permitting the establishment of endowments has encouraged Ecuador, Panama and Paraguay to move ahead with debt proposals.

Question. Has A.I.D. granted funds for debt-for-nature swaps in countries other than Madagascar? Is A.I.D. planning to participate in other swaps? (If yes, what countries are being considered?)

Answer. In June 1988 A.I.D. was a minor partner providing $45,000 towards a $2 million debt-for-nature swap in the Philippines. The $1 million Madagascar grant was signed in August 1989, and in April 1990 CARE signed a $3.5 million debt swap agreement with Ecuador to protect the environment and the lives of the impoverished farmers who depend on it. An A.I.D. grant of $1.75 million will fund half of the purchase price.

A.I.D. is planning to participate in additional debt-for-nature activities in Ecuador, the Philippines, Panama, and Paraguay. Panama may also benefit from the new authority, depending on the outcome of the supplemental legislation currently before Congress.

Under the proposed Philippines Natural Resources Management Program up to $25 million will be programmed for debt-for-environment swaps for nongovernment organization (NGO) conservation activities. It is expected that a consortium of U.S. and Philippine NGOs will administer an endowment funding individual activities under rules established by A.I.D.

Under a proposed program with the University of Rhode Island, a debt-for nature swap supported by a $127,000 A.I.D. grant will provide the resources to fund an environmentally sound coastal resources management project in Ecuador.

Question. There have been problems carrying out the reforestation provisions of conservation agreements established in the first debt-for-nature swap program in Bolivia in 1987.

Does A.I.D. have a mechanism for ensuring that the provisions of A.I.D. sponsored debt-for-nature swaps will be carried out once the funds are allocated and the swap takes place?

Will A.I.D. personnel be involved in carrying out provisions of such debt-for-development swaps or somehow monitoring projects carried out with A.I.D.

Answer. No A.I.D. grant funds were provided to Bolivia in support of the July 1987 debt-for-nature conversion spearheaded by Conservation International. A.I.D. agreed to permit the use of the equivalent of $150,000 of Government of Bolivia owned P.L. 480 local currency to support a management unit responsible for carrying out the environmental programs. Administration of the operating fund rests with the Ministry of Agriculture and the Bolivian NGO designated by Conservation International.

Debt-for-nature programs involving A.I.D. funds are carried out by U.S. PVOs or NGOs (under grants or cooperative agreements) with established track records. Normal A.I.D. oversight is exercised by A.I.D. personnel. Further, specific guidelines have been prepared and circulated which provide, inter alia, for written agreements between the contracting parties, pre-agreement on the purpose and terms of debt purchase and retirement, prior A.I.D. approval of the proposed transaction and purchase price, and special quarterly reporting.

Question. What additional funds have been sought to carry out A.I.D.'s involvement with debt-for-nature swaps?

Answer. A.I.D. generally seeks contributions from the nongovernmental organizations participating in the swaps. For example, in the proposed Panama swap, A.I.D. is proposing a $10 million grant which will be increased by a $5 million contribution from The Nature Conservancy. In Paraguay, A.I.D. is proposing a $500,000 grant which will be added to $1.7 million from The NATURE Conservancy.

A.I.D. Policies and Procedures for Pesticides

Question. In 1987, this Committee directed A.I.D. to examine its capabilities for assisting developing countries to properly use agricultural and industrial chemicals. A research paper on this topic was prepared for the agency by the Conservation Foundation. Several recommendations were made for improving the agency's ability to address newly emerging environmental concerns.

What changes have been made in policies or procedures for furnishing pest control products to developing countries?

Answer. Because the Conservation Foundation Report states that A.I.D.'s current policies are "exemplary" and have "set a precedent for other donors", A.I.D. has made no recent changes in policies concerning the provision of pesticides in A.I.D.-supported activities. A.I.D. continues to adhere to the regulations set forth in CFR 22, part 216, which require a thorough review of potential environmental impacts prior to support for the procurement or use of pesticides.

However, the same report indicated that while A.I.D.'s policies are beyond criticism, more could be done to ensure effective implementation. One effort presently underway in the Agency is preparation of a document entitled "A.I.D. Pest Management Guidelines". This document is being designed to provide additional guidance to field Missions on the implementation of economically and ecologically sound pest management strategies, and will include a chapter clarifying A.I.D. regulations on pesticides.

In addition, the A.I.D.-funded Consortium for International Crop Protection has a new pesticide information system that can provide instant updated details on pesticides registered by the EPA, including information on restricted use and residue tolerances. This service is provided at no cost.

MANAGEMENT OF NATURAL RESOURCES BY A.I.D. IN ASIA AND THE NEAR EAST

Question. When will the natural resources management strategy for the Asia/Near East region be cleared and implemented?

Answer. A draft of the environment and natural resources strategy for the Asia, Near East and Europe (ANE) region will be circulated for outside comment in mid-May, 1990 and will be in final form for implementation by July 1, 1990.

Question. Is protection of biological diversity a high priority in this strategy? What is the status of biological diversity programs in Asian and Near Eastern countries?

Answer. The ANE strategy identifies the destruction of tropical forests and biological diversity as one of the five key environmental issues in the region. Activities to conserve biological diversity are increasing in number as is the level of funding. In FY 1991, the ANE Bureau anticipates grant funding at $11 million, whereas in FY 1989 the funding level was $2.6 million.

Question. Are environmental projects in the Asia and Near East region being cancelled because they are not considered to be in accord with Bureau economic growth priorities?

Answer. One environmental project—a watershed management project in Morocco—was deferred to permit further analytical work this year on key technical and policy issues. The ANE Bureau anticipates that this work will lead to a new project to address water management issues in the near future. No environmental projects have been cancelled.

Question. Will energy alternatives and environmentally sound energy production systems be a high priority in this strategy?

Answer. Energy conservation, efficiency and promotion of renewable energy options are a high priority in the Environment and Natural Resources Strategy, along with environmentally sound technologies.

ENVIRONMENTAL STRATEGY FOR ASIA, THE NEAR EAST AND EUROPE

Question. The Committee understands that A.I.D.'s Bureau for Asia, Near East and Europe is in the process of preparing an environmental strategy that will soon be ready for discussion with the Congress and the environmental community. How will this strategy relate to that adopted last year by the Bureau for Africa?

The environmental strategy for the Latin America and Caribbean is based on the individual Country Environmental Profiles that have been prepared and updated over the past ten years. Is the ANE strategy based on any such documentation?

Answer. The Bureau for Asia, Near East and Europe (ANE) is using an approach to the development of its environmental strategy that builds on the range of experience gained by the other A.I.D. bureaus. The ANE Bureau used available background information, such as country environmental studies, supported by A.I.D. or other donors, as well as a specially commissioned background analysis of the major regional issues, similar to the approach taken by the African Bureau. The ANE strategy emphasizes the need to continue to collect, analyze and update information on the status and trends of environmental conditions on a country-by-country basis.

U.S. ASSISTANCE TO THAILAND FOR PARKS AND REFORESTATION

Question. What forestry projects are supported by A.I.D. in Thailand? What is A.I.D.'s contribution to their budget? How many of these projects are related to development of a forest industry and how many address reforestation of denuded lands so as to prevent a repetition of last year's floods and landslides, in which hundreds of people are said to have "died of deforestation"?

Answer. In FY 1988 A.I.D. initiated a new, six year Management of Natural Resources and Environment (MANRES) Project which is addressing a number of forest conservation and management issues, but not the development of a forest industry. Specifically, the MANRES project is assisting the National Parks and Wildlife Conservation Divisions of the Royal Forestry Department to improve the administration, protection and public education services of Thailand's national parks, wildlife sanctuaries and other protected areas. In response to the disastrous floods and landslides in southern Thailand in 1988, A.I.D. provided a team of specialists to examine the unprecedented level of ecological damage and prepare a framework for risk reduction, restoration and disaster preparedness. That report, "Safeguarding the Future: Restoration and Sustainable Development in the South of Thailand," issued in 1989, provided a range of actions for the government of Thailand's consideration. It was also useful in the context of the devastating November 1989 typhoon.

Question. Thailand is the largest importer of pesticides in southeast Asia. Some hill tribes spray their crops so often that they will not consume the fruit themselves, but save it for sale. In 1985, 25 people died and 2400 were sick as a result of pesticides. Even vultures—the garbagemen of the tropics—are dying from the heavy spraying. What projects does A.I.D. support to wean farmers from an excessive and unsafe reliance on pesticides?

Answer. A.I.D. has supported a pesticide consultant in Thailand and the training of Thai participants in pesticide management and non chemical controls. Regional workshops for Southeast Asia were held in Bankgok in 1987 and in Manila in 1989. One of the major issues regarding excessive pesticide use is the provision of subsidies. This is an area of government policy that A.I.D. believes will be addressed in the future.

Question. Thailand has displayed a commitment to the conservation of natural resources that is not matched even by many developed countries. Does A.I.D. agree that Thailand ought to be unusually fertile ground for U.S. efforts in assisting conservation? What are the competing priorities for funding or other assistance in the area, and what would happen to conservation efforts in Thailand if A.I.D. assistance were withdrawn?

Answer. A.I.D. agrees that Thailand is an important country for assistance in conservation of natural resources. That is why we have planned a $5 million component of the MANRES project that addresses biological resources conservation. The MANRES project continues through FY 1994. Although the A.I.D. program in Thailand is being restructured to reflect reduced funding and staffing levels, we anticipate that environment and the conservation of biological diversity will continue to be an important element of any future program.

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